S. Hrg. 99-508

IMPLEMENTATION OF THE 1984 DEFENSE PROCUREMENT LEGISLATION

HEARINGS

BEFORE THE

SUBCOMMITTEE ON DEFENSE ACQUISITION POLICY

OF THE

COMMITTEE ON ARMED SERVICES
UNITED STATES SENATE

NINETY-NINTH CONGRESS

FIRST SESSION

OCTOBER 17, 29; NOVEMBER 7, 13, 1985

Printed for the use of the Committee on Armed Services

56-769 O

U.S. GOVERNMENT PRINTING OFFICE
WASHINGTON : 1986

S201-22

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IMPLEMENTATION OF THE 1984 DEFENSE PROCUREMENT LEGISLATION

THURSDAY, OCTOBER 17, 1985

U.S. SENATE,
SUBCOMMITTEE ON DEFENSE ACQUISITION POLICY
OF THE COMMITTEE ON ARMED SERVICES,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:08 a.m., in room SD-138, Dirksen Senate Office Building, Senator Dan Quayle (chairman) presiding.

Present: Senators Quayle, Goldwater, Warner, Bingaman, and Glenn.

Staff present: Alan R. Yuspeh, general counsel; Alan L. Chvotkin, counsel; Jonathan L. Etherton, professional staff member; and Marie Chaillet, staff assistant.

Also present: Gerald J. Smith, assistant to Senator Goldwater; Alan Ptak, assistant to Senator Gramm; Edward McGaffigan, Jr., assistant to Senator Bingaman; Milton D. Beach, assistant to Senator Glenn; and Bill Hunter, assistant to Senator Quayle.

Aslo present: Bill Montalto, Small Business Committee; Jeff Minsky, Government Affairs Committee; and Doug Mitchell, Government Affairs Committee.

OPENING STATEMENT BY SENATOR DAN QUAYLE, CHAIRMAN

Senator QUAYLE. The subcommittee will come to order.

This morning the Subcommittee on Defense Acquisition Policy begins a series of oversight hearings on the implementation of the 1984 procurement legislation affecting the Defense Department.

During these hearings we will receive testimony on the status of DOD's implementation of the Competition in Contracting Act of 1984 (Public Law 98-369), the Defense Procurement Reform Act of 1984 (Public Law 98-525), and the Small Business and Federal Procurement Competition Enhancement Act of 1984 (Public Law 98-577).

Over the past 2 years, an unprecedented amount of new legislation has been enacted to alter the defense acquisition process. That trend has continued this year with the inclusion of the Defense Procurement Improvement Act of 1985 in the Department of Defense Authorization Act of 1985, upon which the House has yet to act.

In all likelihood, we will see further legislative initiatives in 1986.

The legislation which has been enacted has already made significant changes in the defense acquisition environment. Fundamental changes have occurred and are continuing to occur in areas such as competitive procurement, technical data rights, warranty requirements, and bid protests, as well as others.

Because of the complex nature of the acquisition system, these changes will have a compound effect on the process. By continuing to propose piecemeal changes to the process, some appear to have lost sight of this fact.

If we are to continue the process of constructive acquisition reform, we must break away from this peacemeal approach and focus our efforts on more comprehensive changes. We need to view the issue of procurement reform from the perspective of general defense reorganization, acquisition work force and the overall weapons acquisition process.

Shortly, I will be making proposals for further reform using this broader approach.

The purpose of today's hearing and those that will follow is to begin building a record on the current state of the process in light of the new legislation which has been and is continuing to be implemented. Because the impact of the recent changes will only be felt gradually, the record produced by these hearings will not be definitive.

However, we will have a preliminary understanding of the effect of the 1984 defense procurement legislation that will be useful as the subcommittee continues its oversight role in the future.

I might add I believe the oversight role is something which is important. It is important that this committee conduct it vigorously. It is necessary for me to understand what we have, the impact of it and how we can establish a good working relationship on the implementation of the act which the Department of Defense has responsibility to enforce.

It is appropriate that Dr. James P. Wade, Jr., the Assistant Secretary of Defense for Acquisition and Logistics, be our lead witness in this series of hearings.

Dr. Wade, as the first incumbent of this newly created position, is reponsible for coordinating acquisition throughout the Department of Defense. He brings the experience of many years of service in the Department of Defense to this new position.

Following Dr. Wade's presentation today, we have scheduled further hearings to receive testimony from the joint logistics commanders, the competition advocates for the services and the Defense Logistics Agency, representatives of other Government agencies, and other outside witnesses.

Before turning to Dr. Wade, I will ask Senator Bingaman if he has any opening comments.

Senator **Bingaman**. I do not. I am looking forward to the testimony. I appreciate your calling the hearing.

Senator **Quayle**. The Honorable James Wade, welcome to the subcommittee. I am sure this is not the last time you will appear here. We have a lot of work ahead of us. We look forward to a very beneficial relationship.

STATEMENT OF HON. JAMES P. WADE, JR., THE ASSISTANT SECRETARY OF DEFENSE (ACQUISITION AND LOGISTICS), ACCOMPANIED BY MRS. ELEANOR SPECTOR, DEPUTY ASSISTANT SECRETARY OF DEFENSE FOR PROCUREMENT

Dr. **Wade**. Thank you, Mr. Chairman and members of the committee.

Again, I would like to start off by noting my personal pleasure to be here with you and your subcommittee in the sense of the opportunity to continue the dialog between Congress and the Department of Defense. Our intent is certainly to improve on the acquisition process as a whole.

Let me first of all introduce on my left Mrs. Eleanor Spector who is my Deputy Assistant Secretary of Defense for Procurement. I think her expertise in the area of procurement will help us in some of the questions we might want to get into.

I would also like to enter my prepared statement in the record and spend a few minutes going through the highlights and spend most of our time in discussion.

Senator **Quayle**. Your full statement will be part of the record.

Dr. **Wade**. Thank you, sir.

We in the Department agree with the thrust of the legislation that was passed last year. However, we would have preferred to accomplish such reforms through the regulatory process as this provides an easier opportunity to make changes to the reforms, if this becomes necessary. But overall, I agree we are together in the context of what we are trying to do.

As to the Competition in Contracting Act of 1984, I think this measure has indeed received the most attention since its provisions are applicable to all Government agencies. I would note here that we conducted training sessions throughout the country concurrent with implementation of this act. Despite this effort, I think I ought to note that the paperwork burden has indeed been increased and there has been some lengthening of procurement leadtime. Although we can see this occurring at this time, the real impact of this legislation will not be known before 1986 at the earliest. This is due to the fact that a large number of the solicitations for our major programs were issued before the April 1, 1985 effective date of the act. The act does not apply to those acquisitions.

At the same time, however, the percentage of the competitive contracts has increased to about 48 percent for the first 10 months of fiscal year 1985 versus 43 percent for fiscal year 1984.

The GAO report issued on the CICA implementation is under consideration.

As to the Defense Procurement Reform Act of 1984, this act is in its final stages of implementation. Interim rules are being issued on technical data.

It is too early to assess the full impact of this legislation and we have had indeed strong commentator reaction on technical data and contractor certification of most favored customer price for commercial type items. The net result of this legislation, I think is still to be determined.

It is also important to note that 30 percent of our acquisition regulations were affected by the 1984 legislation and this followed immediately behind our issuance of the FAR that completely reorganized the acquisition regulations.

We need to resist further procurement reform legislation that addresses problems at the margin until we have had time to digest what has been enacted and determined what the full impact is.

We are fully aware that the majority of this current legislation addresses the so-called horror stories of spare parts. It is important for us to note with the committee that these horror studies are not indicative of the current system as a whole. In many ways a sense of proportion has been lacking in the context of how we have handled this matter.

Despite the many erroneous perceptions coming out of the spare part stories, there is indeed room for procurement improvement. However, we need to focus our time on what areas need to be improved rather than work entirely at the margin on micro changes.

We are indeed in an era of change, technology is moving very fast, our industry is moving fast, the culture behind it is moving fast.

We need to spend time understanding what the core of the problem is and work on that rather than spend time at the margin making micro changes. I would like to address that further, later during my discussion with you this morning.

DOD has underway a number of acquisition improvement thrusts. For example:

The emphasis on producibility;

The question of factory modernization has to be addressed;

Increased competition is a continuing effort;

Increased scrutiny of overhead costs;

Increased auditing and surveillance and the management attention being given in this regard; and

Indeed, our willingness to act as a tough customer when the situation so warrants.

The bottom line, in my opinion here, Mr. Chairman, is this administration has indeed made great progress over the last 4 years. We recognized early that the defense management is a demanding and difficult task and we put our priority attention to that in that regard.

We indeed discovered many of the examples of wastes and fraud and we appreciate a certain amount of public misconception in this regard. I would note here if we go back and review the record, we have a record of accomplishment, but again more can be done in the future.

I believe that we need new directions and we need new approaches. If I had to say what the bottom line is as we look to the future, quality should be at the top of our agenda. Quality must regain its preeminence as far as the product that comes out of the DOD; as a matter of fact, the product that comes out of our country as a whole. Minimal acceptable quality is no longer sufficient as far as the Department of Defense is concerned.

Quality is indeed as important as obtaining the lowest price for a given acquisition. We have to keep that in front of us. We ought to spend more time, more priority on competition for excellence rather than focus totally on competition for price.

The DOD is pushing for the use of the latest technology in contractor manufacturing capabilities. I think we are beginning to see some payoff here. For example, flexible manufacturing systems offer great potential in the DOD environment in which we have to produce a smaller number of piece parts.

We have $100-plus billion per year in our procurement budget. This offers ample opportunity for DOD to play a leading national role in the modernization of our domestic production capability. We would expect a commercial effort as a spinoff from the advantages we can offer the country as a whole.

For example, in numerically controlled machines in which we have been successful in the past, and in the area of microelectronics.

So, in order to promote these objectives, we are reviewing our pricing and our profit policies. We are seeking to improve defense and our contractor manufacturing expertise and consider again emphasizing our manufacturing, production, maintenance, and support processes as part of the overall DSARC and source selection procedures.

As to the important aspect to the early up front planning of new weapons systems, the design and development process may not be suitably optimized to cost tradeoffs. For example, so far we have had only limited interaction between the users, developers, and the manufacturers.

I think we can see a need for improvement in this area. Further, I think everybody is well aware of the fact that the last 10 percent of performance can drive 30 percent of the total cost of the weapon system. We need better accountability of the specifications and requirements tradeoff in the sense of how they best match the use of the objective to the program as a whole.

Our streamlining initiatives have indeed been successful as a start. We have something like 18 major programs underway. We intend to expand this in the future.

I would like to focus on a very important observation that I believe has a bearing on our work force. The Department of Defense is indeed a high-technology Department. Industry that supports the Department of Defense is indeed an equivalent high-technology work force.

With the Department of Defense, although we currently have a good work force, I think in today's climate they do not get the credit they deserve. At the same time there is ample room for enhancement and improvement of the work force as a whole.

Our professional work force has to be high-technology if it is going to do the job of meeting the high-technology work force in industry and at the same time providing the assurance that the product that we turn out in the Department of Defense fulfills the requirements of the national defense.

This is an extremely important observation, a point that I would like to raise with the committee because, in my opinion, it is the people work force that is the infrastructure for the whole process.

We must install a sense in this work force that the money the American people give to us to spend for our new weapon systems is money that must be spent wisely. We need to look forward to changes in our pay structure, changes in our rotational programs, training, more flexible personnel procedures, looking to the DOD as a whole in order to improve.

This is an area, an important area, where I think cooperation between Congress, the DOD and industry is required if we are going to see significant progress over the coming years.

I think the work force has to stress what I would call DOD solutions to our problem rather than individual service solutions. We have to have improvement in the acquisition process and define lines of authority, responsibility, and accountability if we are going to optimize the kinds of money required to provide an adequate assured deterrent force.

Another important aspect here is the relationship between the Department of Defense and industry. I think that up to now, we have placed too much attention on the use of criminal penalties as a result of perhaps poor performance.

It is indeed true, in my opinion, that our defense industry has not been sensitive enough to the problems that we face in providing an adequate deterrent program. We have continued, in my opinion, a business-as-usual approach.

Our industry has to be sensitive to the problem of working the problem with the Department of Defense. I intend, and we intend, to challenge industry in the future to develop more aggressive programs for working in true partnership with us.

At the same time, many of these procedures and these regulations that we have, which provide criminal penalties, have a down side. I think if they go too far, you will find more people leaving this business who truly are interested in working in national defense and leaving room for people who would like to take a risk of criminal penalties.

In summary, Mr. Chairman, I would argue and observe that a mandate for change exists today. Our defense acquisition process is indeed very complex.

Our solutions need to be constructive, they need to be systematic, they need to be sensible and I think they need to also be tough and feeding on each other so that we solve this problem once and for all.

Congress and the Department of Defense and industry together, all have roles and responsibilities in solving the problem. We must solve it together as a corporate body.

In summary, we in the Department will continue to work with the Congress and the Packard Commission, with the most important objective in mind of regaining and maintaining the confidence of the American people that, one, we can spend their money wisely, and we can go out and equip our forces efficiently with the kind of equipment we need to maintain our freedom.

We have to acquire effective equipment. It has to be affordable, it has to be efficient; also, it has to be on time.

Thank you, Mr. Chairman.

[The prepared statement of Dr. Wade follows:]

PREPARED STATEMENT BY HON. JAMES P. WADE, JR., THE ASSISTANT SECRETARY OF DEFENSE (ACQUISITION AND LOGISTICS)

Mr. Chairman and members of the committee. It is a pleasure to be here to discuss the legislation enacted last year on procurement and our implementation. I want to thank Senator Quayle for this opportunity to continue a dialogue between Congress and the DOD, and for his interest in effecting procurement reform. Without question, the legislation enacted last year was the most substantial change to procurement law since the enactment of the Armed Services Procurement Act of 1947.

In general, we agree with the legislation. To a large extent the legislation laid a statutory base to certain existing procurement policy and the initiatives we have taken since 1981 in procurement reform. While we would have preferred to perfect the procurement system, including manpower, requirements, quality and process through regulatory reform, we are pursuing the course of action that Congress has laid out.

However, we must be cautious about laying down statutory rules that may inhibit our flexibility to take advantage of research and technology advances. Besides our people force, our single most important advantage to meet the ever changing threat to our security is to optimize the application of our scientific advances in our military equipment. We know only too well that if we wait to apply these advances until they are perfect, our potential adversary will shortly be on a concurrent counter measure and our advantage may well be lost.

The Competition in Contracting Act of 1984 (CICA) has received the most attention in and outside the Government since its provisions are applicable to all Government agencies. It was implemented in full on April 1, 1985. It requires full and open competition with seven exceptions. Single sourcing must meet one of the exceptions and requires justification and certification by the contracting officer as well as approval above the contracting officer through the senior procurement executive if over 10 million dollars.

Training sessions were instituted throughout the country concurrent with our implementation. The real impact of this act will occur in fiscal year 1986 as a large number of solicitations for major programs were issued before April 1, 1985 and thus the act did not apply.

We have significantly increased the percentage of competitive contracts, to about 48 percent for the first ten months of fiscal year 1985 versus 43 percent for fiscal year 1984. Our objective is to pay a fair and reasonable price for quality supplies and services. Competition is one method for achieving that objective where it is practicable and possible.

Effective dates for the implementation of the many provisions in the Defense Procurement Reform Act of 1984 were strung out over a year. Fortunately Congress provided a full year for implementation of most of the provisions with substantial impact. These substantial provisions either have been fully implemented or are in the final stages of implementation. Interim rules are being issued on the key provisions concerning the acquisition of technical data, validation of technical data, and identification of vendor sources by contractors effective tomorrow—October 18, 1985. Efforts to implement many of these provisions have been complex. For example, coverage concerning technical data requires careful balancing of the need to acquire the rights in technical data for the purpose of enhancing competition while not stifling the initiative of American industry to develop leading edge technologies without Government funding. Because many of the provisions are similar or identical to provisions enacted in the Small Business and Federal Procurement Competitive Enhancement Act of 1984, applicable to civilian agencies, a close working relationship between the Defense Acquisition Regulatory Council and the Civilian Agency Regulatory Council was required. It has been an extensive task. Since our implementation of the major provisions has been recent or is about to occur, we have no real assessment of their impact. However, the provisions are quite similar to initiatives that we have taken over the past several years and our personnel should be in a position to absorb them.

There have been strong commentator reactions to our proposed rule on acquisition of technical data as well as our rule recently issued on contractor certification of most favored customer price for commercial type items. Collectively, commentators believe that we went beyond the statutory language of what is realistically doable. Upon reflection, we agree with the sense of the reaction and will revise our implementation to be in accord with the statutory provisions.

Over 30 percent of our regulations were affected by these statutory enactments following immediately behind the issuance of the Federal acquisition regulation (FAR) and Defense FAR supplement in April 1984. It is a most difficult task for our procurement personnel to absorb these wide-scoped changes and yet continue to purchase supplies and services to clothe, feed, house, train, and provide weapons to our field forces. I am somewhat amazed that there has not been a major rupture in the acquisition process.

The quality and capability of our procurement personnel is high, but we must do more to enhance and enrich this career field so that we have top-flight professionals serving the Government and the taxpayer.

I would strongly recommend to the committee that it resist further procurement reform legislation until we have had a year or two to assess the impact, improvements, and deficiencies of the legislation enacted. The pending DOD authorization bill for fiscal year 1986 contains a number of additional procurement reforms. I think this is unfortunate, but I can understand the congressional frustration that something further was needed with a daily dose of some mistakes or poor judgment being revealed. With almost 15 million procurement transactions a year even if we were 99.9 percent perfect, we would still have 15,000 actions we would like to do over.

I suggest that the committee focus on matters that will reduce the paperwork, administrative burdens, and cost of defense purchases. We believe raising the statutory threshold for the application of publicizing solicitations to $25,000 is in keeping with the small purchase threshold of $25,000 and is most appropriate.

The Commission on Government Procurement in their report of 1972 identified over 4,000 statutes that impact on acquisition. More does not currently seem to be the answer. DOD working together with the Packard Commission and Congress must condense some of these statutes and make joint improvements.

I believe the vast majority of the current legislation is based on the premise that the DOD needs assistance in reforming the way we purchase systems, equipment, and materiel. The impetus for many of these reforms has been the seemingly daily "horror stories" on hammers, coffee pots, or other spare parts. Whether they are individually justified or not, these stories fortunately are not indicative of our current acquisition system as a whole. A sense of proportion, as I alluded to earlier, is lacking. Questions that arise on the wisdom of this legislation stem from doubts that the legislative process lends itself to management system reform and the minutia that can be entailed.

But while I am convinced we are not doing as badly as some perceive us to be, I am equally convinced that there is room for significant improvement. And while we in the DOD are operating in an era of change, no one can doubt that our society is also rapidly changing. Management styles and approaches are changing. Perhaps even greater changes are taking place in technologies and in the workplace. A tremendous debate continues as to the types of industries and technologies, traditions, and culture that will make up our "post-industrial" society as the microchip instantaneously transforms our lives.

There are a number of actions the DOD has already taken in a wide variety of areas that will help lower acquisition costs, promote productivity and quality improvement, and ensure the best possible work force in the procurement area. Some actions involve overcoming impediments or obstacles that, for one reason or another, are present in our current system. They include our emphasis on producibility, factory modernization, increased competition, scrutiny of overhead costs, increased contract auditing and surveillance activities, and continuing willingness to act as a tough customer.

During the past four years, we have made great progress in rebuilding our national defense and in confronting the challenge of effective defense management. We've accomplished a great deal, and we have much to be proud of. When the administration began its activities, the problem of defense management we knew would be demanding and difficult. There are various barriers to efficient management, that in the past stubbornly defied our efforts to remove them. While overseeing our much-needed defense build-up, Secretary Weinberger has done a tremendous job at ferreting out waste and fraud. But a public misconception has developed from all of this, a misconception born, at least in part, of a drumbeat of propaganda and demagoguery that denies the real accomplishment of these last four years. The situation reminds me of an old saying, "Don't clean the skeletons out of the closet. They'll accuse you of murder."

Well, we've ignored that advice in this administration. When Secretary Weinberger came to the Defense Department, he pledged to improve the efficiency and effectiveness of defense management. He went straight for the skeletons in the closet, and there were many. Secretary Weinberger has put in place many management reforms, and more proposals are being considered, both by the Department and Congress.

And although we have made and are making progress, there is one item with which I can agree with many of the defense critics—that much more remains to be done. The challenges and opportunities that confront us require a reevaluation of our direction and new approaches in a number of areas.

Quality is on the top of my agenda for the future. Historically, quality has been the hallmark of American service and products. In recent years this image has been tarnished. Management in the United States has traditionally relied on the concept of an "acceptable level of quality." This has tended to be the minimal amount of quality to remain competitive, or in DOD terms of reference, to satisfy minimal contractual requirements.

This concept of minimal quality must be replaced with a philosophy of continuous quality improvement. In DOD acquisition, competition is too frequently based just on price, and an "award to the low bidder" mentality is too pervasive. As long as this persists, there is no reason for contractors to make quality improvement a way of life. However, we intend to find new ways to consider quality history in the source selection process and to reward high quality performance. We plan to move away from defining equipment requirements in minimally acceptable terms to a system whereby the best quality equipment at an acceptable price is our recognized objective.

There is little question that the DOD push to make greater use of the latest technology and manufacturing systems in defense contracting is paying off. Recent advances such as flexible manufacturing systems offer even greater promise. These computer-controlled and integrated machines, work stations, transfer mechanisms, and tooling allow production of a variety of products in small numbers and are ideally suited to the DOD manufacturing environment—where batch production methods are used extensively, quantities are frequently small, deliveries are over a period of time, and engineering changes frequently occur.

Perhaps most significantly, with an annual procurement budget in excess of $100 billion, the DOD is playing a leading national role in promoting manufacturing and productivity improvement important to the economic revitalization of our Nation. By the nature of our high level of contractual expenditures, the DOD has tremendous leverage in promoting manufacturing and productivity improvement that can be of benefit not only to the Department but also the commercial industrial base which is ultimately the source of our defense capabilities. We're confident that the results of our current efforts can have the same impact in the commercial sectors as the classic examples of the role the DOD played in the development of numerically controlled machine tools and micro-electronics.

I am looking for ways to revamp and restructure existing programs and policies to further promote this objective. Pricing and profit policies will be reviewed in this light. Cost accounting procedures may need to be revised to reflect the ever decreasing direct labor component of system costs. Manufacturing expertise of DOD and contractor personnel need to be increased.

The decision points that occur during source selection and the Defense System Acquisition Review Council processes are where the DOD has the greatest degree of influence over both contractors and program offices. Manufacturing, productivity improvement, and quality must receive the same attention as system performance in these arenas.

The current system design and development process is not oriented to emphasize cost tradeoffs and optimization. There is insufficient interaction between users, developers, and manufacturers. Requirements are not continually examined as new information becomes available supporting technical alternatives or more cost-effective approaches. The last 10 percent of performance can end up driving 30 percent of the cost. Clearer lines of accountability and visibility for the specifications and requirements match are needed in the early phases of a program.

We have made progress in our streamlining initiative to reduce or eliminate contract requirements that add costs in excess of benefits. But to date streamlining has been directed at the productivity on the past of DOD personnel (driven by the principle of risk aversion) to impose all sorts of management systems and demand mountains of paperwork. We need to expand the streamlining concept to include optimizing functional requirements. We are finding new ways to establish baselines and cost caps around which we can make performance and quantity tradeoffs.

The DOD is and must remain a "high tech" department. We cannot function in this environment without an equivalently capable work force. Indeed, they provide the foundation of all of our defense acquisition improvement efforts. Initiatives and legislation do not in themselves solve problems. Direction and goals may at times even seem conflicting. In reality, real progress is made by actually doing correctly all of the detailed work associated with these responsibilities. Proper implementation is the key, and the acquisition work force—from contracting personnel to engineers—have the most important and difficult job.

We currently have a good work force—and it bothers me that in today's climate they frequently don't get the credit they deserve. But there are a number of actions we can take to enhance our acquisition work force. We must also instill all individuals (extending to defense contractor personnel) better discipline and a sense that it is "our" money being spent and not someone elses. We also need superior, better qualified people, changes in rotational programs, training, and more flexible personnel procedures are needed to attract and retain a talented cadre of professionals with the proper backgrounds and experience. This is an excellent example of an area where cooperation between the executive and legislative branches will be critical if needed changes are to be made.

We must also take a serious look at the DOD acquisition structure. An energized procurement work force needs to be matched with a modern acquistion management system for optimal results. Increased attention to addressing needs from a joint perspective, stressing DOD solutions rather than service solutions, should be considered. In any case, a system with more clearly defined lines of authority, responsibility, and accountability has a far better chance of success.

Much has been said about the proper relationship of the DOD and industry. It is usually characterized in terms of being too adversarial or too incestuous depending one one's viewpoint. We have to be very careful that neither extreme is a reality.

One concern I currently have is that we may be placing too much emphasis on the threat of criminal penalties. We don't want to end up in this situation where crooks are the only people willing to do business with the DOD—since they may be the only type oblivious to the risks.

I am equally distrubed by the impression that industry has not been sensitive enough to the problems we are facing. A "business as usual" atmosphere has been too pervasive.

In the months ahead, I will be challenging industry to develop an aggressive program of their own aimed at prodcutivity improvement and acquisition cost reduction. Industry participation, action, and leadership are essential parts of the improvement process.

There is a mandate for change today. We have the chance to pursue reforms that perhaps in different times would have been considered too difficult, drastic, or politically impossible. However, the subject of defense acquisition is a complex one that defies quick fixes and simplistic solutions. Change needs to be pursued in a constructive, systematic, sensible, and positive fashion. Congress, the DOD, and Defense industry all have roles and responsibilities in this regard.

I will continue to work with you and the Packard Commission in a mission that is vital to the security or our country. The objective is to regain and maintain the confidence of the American people in our ability to perform the task of acquiring effective equipment for our military forces in an affordable and efficient way.

Senator **QUAYLE**. Thank you very much, Dr. Wade.

We will limit the first round of questions to 10 minutes.

I congratulate you on putting a special emphasis on quality. I think that really speaks for itself. I certainly am one that supports that as being of the highest priority.

I will break down my questions into two parts. One is general oversight and in the second, I will try to extract from you some of these new directions in a little bit more detail than you have described thus far.

I gather from your written testimony and your statement that you are generally satisfied with the procurement reform legislation that has been passed in the last 2 or 3 years, although on a couple of them you mentioned it is still too early to tell.

I guess I perceive that you are generally satisfied with the direction that they are going in and you feel that, there is not going to be any difficulty in implementing those pieces of legislation.

Is that correct?

Dr. **WADE**. Yes, sir.

Senator **QUAYLE**. I also gather that you are not making any request that any laws that have been passed over the years should in fact be repealed.

Is there anything on the books that you would like to see repealed?

Dr. **Wade**. No, sir; not at this time. I believe much of the legislation that was enacted follows what we had been talking about doing in the Department.

I believe we need some time to see how this legislation will affect us. In an overall general sense, it appears very helpful and we are satisfied and supportive of the legislation.

Senator **Quayle**. If that is the case, then we will continue to work with you in an oversight capacity. I think it is very important and if things come up that you want to discuss or bring to our attention, feel free to do it.

Right now the record will show that you are generally satisfied with the results of the legislative process working with the executive branch and your relationship with the contracting community?

Dr. **Wade**. Yes, sir.

Senator **Quayle**. That gets me to the second part of my question.

I notice you said that we need to have DOD solutions rather than service solutions. I wrote that down.

As you know, Chairman Goldwater and Senator Nunn yesterday unveiled a very comprehensive, probably the most comprehensive work on military reorganization in the history of this country. Within that recommendation there were some specific concerns expressed in the area of procurement.

One of the problems that they suggest needed some attention, and I certainly concur as I think you have also expressed in your statement favoring DOD's solutions rather than service solutions, is the inadequate coordination of procurement policy within the Department of Defense.

My first question is: Do you believe that there is presently room for improvement in the coordination of our policy within the Department of Defense and, if so, could this coordination be viewed as the sort of streamlining proposal that you mentioned as more of a DOD solution rather than a service solution?

Dr. **Wade**. Mr. Chairman, in reference to this recent study that has been released, since I have not seen it, I would prefer to address the question in the context of how you stated the question.

Let me focus on the area of acquisition. I think, first of all, we should not denigrate the equipment we have turned out as it has been superb equipment as demonstrated by performance in the Baaka Valley, of F-16's and F-15's. I think that scored as a sign to everybody in the free world.

But I would also note here that technology is moving very, very fast. I think that the technology we have in this country is superior to what is available anywhere in the rest of the world.

In order to optimize this technology, I think that this calls for increased attention to what I would call a joint approach. I think you know I have been deeply involved in this in the past 4 or 5 years and we have had signs of major success in the Department in this regard.

It is not the fact that we have not been doing this. However, it is an area where we can further improve both in the context of front end planning, where I really think you have to focus a good deal of your attention, and acquisition of the material itself.

For example, in the area of some of our major weapons systems like AMRAAM, the mere fact it is a joint program between the Air

Force and the Navy will save you on the order of like $1 billion in R&D.

Due to economies of scale, you get savings in that sense.

There is another point to be made, however. That is that rather than the more narrow interest of a service trying to optimize the solution of their needs, you need to be careful and look at what the requirements are from a DOD-wide perspective and see whether or not the solution can provide an even more enhanced baseline as far as our national security is concerned.

I think that the answer to your question is that we have done well, but we need to do a lot better and more attention is required in this regard.

Senator **Quayle**. In getting the process to work better, going back to your statement of the DOD solution and the example that we just used, I gather that you would like to see a strengthening of the role of DOD, and OSD in some of the procurement policies that would affect the way the situation is now organized and the way people report.

I would also point out I think this is the direction of the Goldwater recommendations. Beyond the inadequate coordination of procurement policy, they also point out the disconnect between our national security strategy and our requirements.

This would go along with what you are talking about, I think, Dr. Wade.

They also talked about commonality of military equipment as something that we can improve upon. They also pointed out the weak management of joint programs. Those are some of the problems.

I guess I will ask, not coming out for or against the recommendations that came out yesterday.

Do we need to work on getting a better connection between our national security strategy and the actual requirements?

Do we need to have more commonality in our equipment?

Do we need to focus more on better management of joint programs?

And is there again the lack of coordination between procurement policy within DOD?

And if those principles are of concern to you, then I guess, again going back to the DOD solution to these problems, that I at least am concerned about, would you agree that these are principles that we ought to address in trying to look at the issue of procurement in this next coming year?

Dr. **Wade**. Mr. Chairman, I would rather reflect further on some of the detailed comments in the report rather than national policy.

Senator **Quayle**. I do not want to get into the details. I have not read the study. We are just digesting it. I am talking about principles. I am trying to get direction, a thematic feeling where you would like to go, where you would like this subcommittee and this committee to go.

The report is timely and it is detailed. Let us leave that report, whether you are for or against it or neutral, and let us talk about general principles and see if we can agree on principles.

Then if we can agree on principles, I think we can probably break this down and come up with some solutions.

Dr. **Wade**. I think we can agree on one principle and that is that we need to do better. As well as we have done in the past, we need to do better.

Again, I would focus on an area that people in the past have felt has been too difficult to address. That is whether or not we can significantly improve upon the acquisition and logistics workforce in the DOD.

I believe at this time that we have an opportunity to increase and improve the professional quality of that work force and that will drive the main process that is used in order to acquire and develop new hardware.

Many people have said the civil service system really cannot be improved in the context of what is required for a high technology force. I refuse to accept that. I believe if you look forward to what can be done to create a really professional system, that many of the problems in the sense of jointness, in the sense of coordination, and in the sense of implementation are going to be solved.

For example, in an area that has attracted a great deal of attention in the last several months, the revolving door problem, I believe if you improve the professionalism of the work force and make it a system and provide a clear career pattern from the youngest person to the oldest, you will find many of these problems will go away.

Although I feel that there is room for improvement, improvement in establishing requirements, establishing the streamlining initiatives, we should still concentrate on the broad national policy matters concerning the acquisition work force. This, I think merits a great deal of attention and great deal of time. We have an opportunity to do some very specific things, in this respect which will make some major improvement in our acquisition program.

Senator **Quayle**. My time is up. I will yield in a moment.

I do not dispute that the work force and the people are key. I do not dispute that we need to focus on the front end.

The only thing we have to try to get a consensus on is what we are going to focus on. Are we really going to say that getting more flexible personnel procedures and a little better pay, that that is going to solve some of the overall problems?

With the front end planning you are getting into some big areas. These are some areas that we would like to pursue. The front end planning is one of the principles that I want to talk about and directly to the point. I will pursue that.

Dr. **Wade**. Mr. Chairman, may I make another comment in this regard?

The part that you are also addressing is a recognition that if you continue to add myriads of legislation that addresses the problem at the margin, you are also going to end up making our program manager a technocrat rather than a manager because he will have to worry about so many small pieces that it will cause him to lose the ability to manage the program.

When you add myriads of legislation on top of each other, we have to worry about what we are doing to the program manager in the context of his ability to manage.

Senator **Quayle**. I agree. If there is legislation that is too burdensome and is complicating the system, we need to know that.

Dr. Wade. That is why I made the comment that we support the legislation, but we would like to learn and digest it before we make our recommendations.

Senator Quayle. That is why I asked the question whether there is something you would like to repeal and your answer was no. There is a problem out there of making people technocrats rather than giving them managerial responsibility.

Chairman Goldwater?

Senator Goldwater. I have just a couple of questions.

What is the attitude now of the Secretary on multiyear contracts? Are you going to keep pushing those?

Dr. Wade. Yes, sir; multiyear contracts are, in my opinion, one of the most important management tools we have for turning out equipment efficiently and affordably.

One thing multiyear does is add stability to a program. You do not have to go into the program every year and worry about the requirement going up and down. You allow the contractor to go out with a long lead time to purchase the materials that are required for the program and produce efficiently at a stable rate.

One has to be careful to do the right kind of calculation up front to see the potential for savings downstream. You have to have an agreement between Congress and the DOD that this is a wise program to move into multiyear. As a general rule, multiyear is a very important tool and we intend to pursue its use vigorously.

Senator Goldwater. I hope you do. I think you can understand that we can save money, for example, if we decide to buy a certain tank and the forces need, let us say for argument's sake, 6,000. If we contract for the whole 6,000 at the existing price, it is going to be a lot better than buying 100 this year, 400 next year, 200 the next year.

I hope you will keep pushing the Secretary on that.

Dr. Wade. His Department is fully supportive of the multiyear program.

Senator Goldwater. Quite a few months ago I was asked down at Oceana to visit with the new team that the Navy had put together. I think they called it a quality competition team.

I was very impressed with that, the fact that the Navy had put together a group of men who knew that the balance of their careers was going to be spent on the one subject of going out to management and creating competition.

As a result of this, the Navy has been able to build, I forget whether it is two or three frigates with the savings in using those taxpayers' moneys.

Is that practice being pushed by the Secretary on the other services?

I know that the Army is getting into it. I want to be sure that the others are also getting into that action.

Dr. Wade. Yes, sir; competition is one of the very high priorities we have in the Department.

I want to emphasize here to you, Mr. Chairman, that competition, though, is not the bottom line. The bottom line is to get the best equipment out affordably and efficiently and better than the other side.

We have seen tremendous payoffs in the last 3 years in the context of pursuing competition. We have, for example, competition advocates throughout the whole Department whose main job is to review programs and competition is being pursued and looked at very strongly.

I want to offer a note of caution. Where we started from 3 years ago was so poor in the area of competition that we have seen tremendous payoffs over the past 3 years and we will see even further payoffs, cost savings in the next couple of years.

But this is not a panacea. It will not increase forever. You can also reach a point where you will put competition in the sense of savings in dollars higher than quality. If we do that, I think, overall, we might hurt ourselves.

That was the point I made earlier, we ought to be now talking about new procedures, new methods looking toward competition, with the bottom line being quality.

We have seen some contracts coming in where some of the people who weigh the value of the contract establish a criteria with both sides go to the bottom line of cost after they are satisfied with quality.

This pushes the contractor into looking toward using more less expensive engineers to win a proposal. You and I know that will end up to be trouble.

We are pursuing this issue. We all must be careful to look for excellence in the program and not purely cost savings.

Senator GOLDWATER. I agree with you. I hope the idea of competition is instilled in all the services even down to the point that we have discussed very briefly on the subject of management.

For example, you bring in a field grade officer and assign him to a desk in the Pentagon or a desk in somebody's factory and say that is your job and in the 3 years, 2, maybe 4, he wants to get back to an operational commmand. That is understandable.

I think you are beginning to find that there are many officers of field grade positions, in the operational side, that would rather be in management. So, I see a tendency and I hope you can study it first and then encourage it, if it is true, to establish this area of management where the officer is trained to do a job and his promotions keep up with his class or his ability. I think that is most important.

Dr. WADE. Yes, sir.

Senator GOLDWATER. The fact that we brought the B-1 in under price and under time, the fact that the Aegis forces are being brought in under time and under cost, point up the fact that with proper management the objectives can be achieved.

Dr. WADE. I agree with that, Mr. Chairman.

I would like to emphasize that I believe we should be spending more time assuring ourselves that the program billets which need to be filled are filled with the most qualified people for that job based on training, experience, and ability rather than where they come from or what their uniform is.

That is a way we can assure ourselves of getting quality product rather than saying here is a billet set aside for a particular service.

Senator GOLDWATER. Thank you very much.

Senator QUAYLE. Senator Bingaman?

Senator **Bingaman**. Dr. Wade, you make a big point here in your statement about the need for more flexible personnel procedures to attract and retain a cadre of professionals with proper backgrounds and experience.

I just happen to have a bill that I have introduced which I hope helps with that. This is Senate bill 1727. It has also been introduced on the House side as H.R. 3480. It is aimed at the Federal science and engineering work force and it is called the Federal Science and Technology Revitalization Act of 1985.

It tries to provide authority to set up a separate personnel system for people with scientific and engineering backgrounds and provide more flexibility in the pay and responsibilities of these personnel.

Have you had a chance to review that or do you have any views on that?

Dr. **Wade**. No, sir; but I will. I have been very interested in what has been going on in this general area since we had a blue ribbon commission which looked at this several years ago.

Senator **Bingaman**. Yes; this is the outgrowth of the report that David Packard did when he was on this White House Science Council's Federal Laboratory Review Panel.

Senator Goldwater and Senator Quayle are both cosponsors of S. 1727.

Dr. **Wade**. I am familiar with that part. I fully support the vital importance of improving the ability of our scientists and engineers in our Federal laboratories to do their jobs.

I would certainly support moving forward with that in the sense of improving that base, but that is only one part of the problem that I am talking about here. We need to look at this issue within the Department of Defense as a system, not as a separate Army, Navy, Air Force, Defense Logistics Agency personnel problem, but a system for the Department of Defense as a whole.

I do not want to slow anything up, but I do think this new approach should be given higher priority than we have in the past.

Senator **Bingaman**. I would be anxious to get your thoughts and particularly any suggestions you might have with regard to broadening the coverage of the bill the way we have introduced it.

Dr. **Wade**. Yes, sir.

Senator **Bingaman**. One of the recommendations that the staff report on defense organization made was with regard to the way Congress functions. The report says that Congress should establish milestone authorizations for major acquisitions.

I gather what is intended is that we would essentially follow the pattern of behavior that the DSARC process now follows. We would approve a program only when it came to these milestones, or only review at that time, and someone would have to come to us with indications that the milestones were not being met or costs or schedule or performance were in trouble before we would have to look at it again between milestones.

In your view, ,is that an appropriate change in the way we do business here in the Armed Services Committee and in the Congress in general?

Dr. **Wade**. Senator Bingaman, I would prefer to read that element in detail. I have learned when you try to pick out and read one sentence out of the context, it will get you in trouble.

If you add another peg point on which the services and program manager have to respond by reporting to members of the Department or Members of the Congress, you will find 40 briefings and meetings getting ready for that. All we would be doing is adding to the length of the acquisition cycle.

My preference would be that we should note that every major program has its own distinct acquisition and the strategy that goes with it. The time to put your attention to the program is not milestone 1, 2, or 3, but milestone 0.

Is the program really required? Is it meeting the need? You should have your senior people sitting down and signing up and moving the program at that time and having the appropriate reviews thereafter to make sure everybody is aboard.

To add a milestone at which we come over and brief the Congress, I think will add to the paperwork. I would be very cautious of how we do that.

Senator **Bingaman**. As I understand the proposal, it would not be to add another layer, but it would be to drop us out of annual authorizing of every program and have us authorize milestones so that we would hopefully review each of these weapon systems less frequently instead of more frequently.

I would say for you to suggest that maybe you would want to read this before you make a comment on it is an unusual request here on Capitol Hill, but I can understand it.

Dr. **Wade**. I like more and more what you are saying, Senator.

Senator **Bingaman**. Let me ask you about another subject. One of the concerns that I know many members of this committee, Senator Goldwater and others have had and I have as well, is that we get the impression that we are getting requests for more weapon systems than we need and more weapons systems than it turns out we can afford.

One example which obviously comes up frequently is, I believe, 16 production lines for naval aircraft. Maybe we can get by with fewer production lines for naval aircraft and we can buy them more efficiently and get more for our dollars.

I would be interested in your reaction as to whether anything you are doing is going to help fix that problem now, if you think it is a problem.

Dr. **Wade**. Yes, sir; first of all, we all appreciate that we have an external threat that drives this problem and in many ways our direct impact on the external threat is not what we would like it to be.

When we say we are buying too many weapons, I do not believe that.

Senator **Bingaman**. I am saying too many different kinds. I am not saying too many weapons. I am saying we could buy more weapons and aircraft if we did not buy 16 different kinds.

Dr. **Wade**. There is that danger. If funding changes and you have to cut back on the quantity you are buying per system, then the cost is going to go up. I think that is the concern.

It gets back to the point that if the budget profile changes dramatically on a year-to-year basis and you cannot plan with any confidence what is going to be, you are going to be in trouble, and we are seeing that right now.

We need more equipment and better equipment. We have to be concerned that if we are buying too many, we had better start shrinking the number. That gets to the point of jointness.

A common DOD approach to some of these requirements should, if done right with quality, save money, provide better equipment, common equipment, that is interoperable. We are working with our allies to accomplish the same thing.

Senator **Bingaman**. It seems to me every year when we get the budget request from the Department of Defense and the President, there is built in, it is obvious, significantly more than we usually are able to authorize.

As we cut back and pare it back to the reality of our fiscal situation, we do not wind up dropping any programs, we just push things out in the future years and reduce the number of each unit that we buy.

Is there any way to fix that problem? Is there any way to do better at either getting more realistic requests out of the Department of Defense and the administration when they come in in January or early February?

Or if we cannot do that, perhaps we can find a way to lop off those lower priority programs and not just wind up buying a little bit less of everything as we go through the process.

Dr. **Wade**. Two aspects. I think, one, in the sense of legislation, biannual procurement approval would help to a great extent because it means fewer programs would be put at risk on a year-by-year basis once approved by the Congress.

Another aspect which I think will be helpful and I mentioned briefly this morning is the modernization of our manufacturing and production capabilities. Flexible manufacturing techniques can, in effect, be able to efficiently produce a broader spectrum in the sense of quantity. For example, 5 aircraft per month or 15 aircraft per month. We won't see these perturbations in the sense of unit cost. We have the opportunity downstream to technically improve this process. At the same time there are other areas that it can be helped legislatively.

Senator **Bingaman**. Let me ask about another area I have been following. That deals with whether or not we really have the in-house, in-service computer capability to store and access the data that is needed to efficiently procure various items, spare parts, and other things.

One of the concerns I have had all along is that it seems we have been very slow, relatively slow, as compared to the private sector in implementing some of the modern computer capabilities that would be essential for intelligent judgments to be made in acquisitions so that you have a good history of what an item has cost before.

I would be interested in your reaction on that as to whether you think we still have a serious problem.

Dr. **Wade**. We had a serious problem, Senator. I think we are well underway toward making a significant improvement. It takes time.

When we started in 1981, I think the base was in terrible shape. Therefore, through the support of the Congress, both by adding about $100 million toward improved computers, and 3,000-plus people to the work force in this area, we are underway toward improving that. It will take 4 to 5 years before we see it fully implemented.

Another area that I think we need to move into is in the area of visual moving information rather than by slow copy. This is a new initiative we have and I think it will revolutionize DOD, but it will be like 1990 before we see an impact.

I would also like to emphasize another part and that is to optimize and get the value out of our more advanced computers, we need a more high tech work force. If you have a people force to match the equipment, you will do a good job. That is why I put more emphasis in this area of looking at acquisition as a corps, a new service, highly professional, and highly trained.

Senator **Bingaman**. I will be anxious to get your reaction as to whether some changes are needed in this bill I referred to earlier to help you accomplish what you have in mind.

Thank you, Mr. Chairman.

Senator **Quayle**. Senator Glenn?

Senator **Glenn**. Thank you, Mr. Chairman.

I was interested in your comments to Senator Goldwater a couple of minutes ago about the idea of quality versus price.

Although I am getting to be somewhat of an artifact in the space program, I am still asked reasonably often what does it feel like to be on top of a booster getting ready to go.

I have a standard answer I have used. I ask the question in return, "How would you like to be on top of this thing built by the lowest bidder on a Government contract?"

It just points out in more personal terms perhaps this idea of quality versus price you are talking about. We cannot always go with just the lowest bidder.

I have been a little concerned that perhaps while I want competition and want the advantages of competition, that we cannot always just go on that basis. You apparently feel rather strongly about that, too, because you mentioned it a couple of times here.

I think on the first page of your statement you make that comment and on page 9 you make the comment again. I am concerned about that, too.

I do not know how far we go with competition and just go with the lowest bidder and how you regulate that. You are going to be one of those who will have to set the guidelines on that.

I would appreciate any comment you might have.

Dr. **Wade**. I fully agree with your concern and I share it. I would just note again that 3 years ago our base point was terrible and we have seen some tremendous payoffs in the sense of competition and saving. I think as managers we are going to have to be careful here.

We are addressing the problem by looking at some new criteria in addition to lowest cost. My goal for the future is execution of our program with the highest quality, not the lowest cost.

Senator GLENN. That is very difficult. You cannot quantify some of those judgments either. That is the problem. You will have to have good, high quality, technically trained people to make some of those judgments. We cannot write laws and rules that cover all of that.

How do you keep competition in black programs? That is a very difficult area. We are finding a higher percentage of our programs going black because we want to keep them classified. Yet we want to keep the advantages of competition and we have some big bucks going into some of those programs.

Dr. WADE. Yes, sir; it is more difficult, it takes increased management attention. The real attention should be up front in the context of what your decision is in the area you are going to go.

We do have competition in these programs. We are putting more attention to it. Let me just say that again because of the nature of the program, increased management has to be given in this regard and we are doing that.

Senator GLENN. On the first page of your statement you talk about statutory rules "inhibiting," and I quote, "our flexibility to take advantage of research and technology."

Could you be more specific on that? I am very concerned about this, too, beause we are getting into programs such as the ATB and the small ICBM.

I spent 10 days last year and 10 days this past summer going all over the country talking to some of our best scientists and technical people regarding our directed energy weapons, lasers and neutron particle beam projectors, and microwave projectors, things like this that are very, very high technology. I am concerned that we not inhibit some of that development by the rules we are making here. You referred to that.

Could you be more specific as to your concerns?

Dr. WADE. There is concern in the context that technology is going very, very fast. In some ways managers are having difficulty dealing with it. They prefer, for example, to wait until next week for some new gadget to come in to put in a new weapon system.

In order to determine the impact that warranties can have on these programs, you have to make a cost evaluation on what you will have to pay for a warranty. Further, it might well be that a contractor could become too conservative in light of his risk under a warranty and pull back on what could be put in a system due to the higher risk associated with some of the new technology development.

So, there is the possibility of people being reluctant to put the most advanced technology into the hands of our forces. We have to be careful about that. We need to put a lot of attention on it. The heart of our deterrent force is superiority in equipment.

When you add these points about additional testing at certain phases of a program, and many more detail briefings to the various layers of bureaucracy, you are going to slow down the process. It is not an easy problem and it gets back to the point that I prefer. Give maximum flexibility to the program manager as a system manager, give him the opportunity to do the job, but make sure he is trained, he is qualified and he has experience and then let him go.

If you put a guy in there who is not trained and you have to have these peg points on him, I think it is a guarantee for disaster.

Senator Glenn. You have been Acting Chief of Research and Engineering?

Dr. **WADE**. I was last year.

Senator **GLENN**. That gives you an optimum background to come into this area of logistics and make some of these judgments.

As you point out in your statement, and I agree with you 100 percent, we need to maximize our technological advantages and keep ahead in that area. We will never outdo the Soviets in numbers of specific things, whether it is people or machines.

If we keep our technology ahead and provide more fire power and capability for each person out there in harm's way, if we ever get in another war, that is our advantage over the Soviets.

Dr. **WADE**. Yes, sir, I agree.

However, I would also add to that in certain instances quantity is as important as quality and by using our technology and putting emphasis on manufacturing techniques and using our skills in that regard, we will enable ourselves to turn out more.

Senator **GLENN**. You indicated our competitive contracts have increased from 43 percent in 1984 to 48 percent in the first 10 months of 1985.

Can you quantify that any more? Can you estimate the dollar savings to the country as a result of this increased competition?

Dr. **WADE**. We do not have precise savings numbers, Senator Glenn. I can, however, provide some data for the record.

We are also experiencing improvement in the number of competition procurement actions. I think that is up to like 70 percent. We are bringing more people to bear on the problem.

[The information follows:]

DOLLAR SAVINGS FROM INCREASED COMPETITION

The level of competition within the Department of Defense has increased over the past several years. The primary goal of our effort to increase competition has been to improve attitudes toward using it wherever appropriate. This has lead to program cost reductions that have, for the most part, already been translated into budgetary savings. Program savings have been recorded by some DOD components. For example, the Defense Logistics Agency estimates their Competition Advocacy Program has saved about $135 million in fiscal year 1985. The Navy estimates that savings from shipbuilding competition totalled $4.4 billion during fiscal years 1983–1985. Air Force Logistics Command estimates more than $500 million has been saved due to several acquisition improvements, not just competition. To put a perspective on other opportunities for improvement, the Air Force Systems Command estimates that more than $3 billion has been saved over the past few years from multiyear procurement, even though the use of multiyear has been somewhat restricted by budgetary considerations during this period.

Senator **GLENN**. Do you have someone studying that?

I, for one, would be particularly interested. We all assume that competition drives prices down and it does. As we got to more contracts being put out competitively, I would be interested in your estimate of how much money is being saved. The ultimate objective is to save dollars.

Dr. WADE. The ultimate objective, Senator Glenn, is to put the best equipment out at affordable prices.

Senator GLENN. I agree, and still do it as economically as we can. I have to get my last hooker in there.

Dr. WADE. I want to note that there has been a tendency to some of these contractors to load up with less qualified people to save money.

Senator GLENN. That does not save money in the long run and it does not do anything for combat effectiveness. I will come around to your argument in a moment.

One other question, Mr. Chairman, that I think is very important. The President has said regarding basic research that if it is worth doing, the contractor will do it and we should depend more on the contractor to do basic research rather than the Government.

That gets us into some real problem areas. We get into wanting companies to do this research, but we say even if you do it on a comingled funds versus private funds, we want to take the proprietary rights for it because it is a contract.

We have a couple of situations in my home State of Ohio. We have written letters back and forth trying to get some of these things straightened out. It is a real problem.

If we are going to encourage people to do research, which we would like them to do, how can we reasonably take away the proprietary rights if it was not straight research done pursuant to Government contracts?

Most of these companies have not that sole purpose in their overall mission. We have been through some of this with the Goodyear people back home. They have their funds. Obviously, they get a lot of funds from the military contracts.

On the other hand, they have a lot of private business, too. When they comingle some of these things, do research and the Government wants to take proprietary rights and put them out for competitive bidding, we are in a real can of worms.

Do you have any comments on that and how do you plan to handle that?

Dr. WADE. I share your concern.

I would also observe we are interested in not only improving the creativity in research in industry, but also in our own Federal laboratories. We had a Nobel Prize winner announced yesterday that comes from a DOD laboratory.

We do not want to stifle the innovative research that is out in industry. We do not want to stifle that research being applied to our own programs. Otherwise, they will continue with their research, but they will not provide it in the sense of their interest in our own programs.

There has to be an appropriate balance between our right to use data to enhance competition particularly where it is developed under Government research funding, and rewarding the innovative initiative of industry.

This presents a difficult problem. However, if it is recognized by both Congress and senior leadership of the DOD, I think we can solve that problem. I think the Competition in Contracting Act recognizes that is a problem. They have addressed it directly.

Now, our job is to manage it with good commonsense.

Senator GLENN. That is a big order.

Dr. WADE. Yes, sir.

Senator GLENN. You are going to have to work on that, as I see it, the whole DOD.

The tendency in Congress right now is in the opposite direction. It is for competition, the lowest bidder and proprietary rights go to the Government because we paid some of the bill. That is the tendency right now.

There is a bad side effect to a lot of that, too. People are not going to put their own money into research if you are going to take the proprietary rights away from them when they have developed something, take their patent rights or whatever.

Warranties are a wholly different matter that we have not discussed this morning. I do not know how to handle a program like that except to say what you have just said, you have to use the best judgment possible in each particular case.

Dr. WADE. You also have to make sure your managers and your scientists and engineers in your Government labs that are helping to manage this issue are qualified and appreciate and understand that issue and they understand being creative and innovative. I think that problem can be solved.

If you have people who are incapable of appreciating that, then you are in trouble because then they become technocrats and bureaucrats.

Senator GLENN. I am very concerned, not just because we had a problem or two back home, but for the country as a whole. You cannot encourage people and then deny them the results of their research, whatever it was.

Yet we cannot go overboard the other way, too, and say on Government contracts the Government does not have some claim on a straight Government type research. That is a tough one.

I hope we are not pushing too hard here in the Congress, Mr. Chairman, in this area of proprietary rights and getting into competition.

Thank you, Mr. Chairman.

Senator QUAYLE. Thank you, Senator Glenn.

Let me ask a couple of questions. One on the issue of warranties.

Are we doing a formal cost-benefit analysis on all of our warranties?

Dr. WADE. I think we are still in the writing phase, Mr. Chairman. I know of your interest. It is a tough problem to develop the right kind of criteria to get some feedback on how well the cost-benefit has been.

You asked for some input from the services. I haven't fully reviewed that. I don't think the bottom line is in on that yet.

I do think it is terribly important to make sure that we do not waste money or waste time.

Senator QUAYLE. You are saying you really do not have any good data now?

Dr. WADE. I do not think we have sufficient data to give us a final answer. I think we probably need another year.

Senator QUAYLE. Do you have a procedure set up to conduct a cost-benefit analysis on warranties?

Dr. WADE. Yes.

Senator **Quayle**. So, you do go through the exercise?

Dr. **Wade**. The services are the ones responsible for their own programs. They go through it. We are in the process of reviewing what they are doing.

Senator **Quayle**. As soon as you get some information, it would be worthwhile to see how it is proceeding.

Dr. **Wade**. Yes, sir.

Senator **Quayle**. There are waiver provisions in there if you so decide to use them.

How many waivers have you used?

Dr. **Wade**. I believe there is one so far. That was in effect when the program was reasonably well underway before the provision became law.

Senator **Quayle**. How many warranties would you suggest there would be? Would it be thousands?

Ms. **Spector**. We are including them in all the major programs that require them. The reasons there have not been more waivers is that we are tailoring the clauses in most cases to make them cost effective. We are writing ones that are not terribly costly.

In many cases they are virtually free. They require correction only after a minimum number of problems are found. So, we have not been seeing waivers. They have been implemented, by and large, sensibly and in several cases with cost-effectiveness analyses.

Senator **Quayle**. So, many of the concerns that the DOD initially had on the warranties are not panning out?

Ms. **Spector**. Not in the sense that we had anticipated. Whether or not they are thoroughly cost effective, we won't know until the hardware is delivered and we see how many corrections we get.

By and large, there has been a sensible tailoring in the ones I have reviewed.

Senator **Quayle**. Dr. Wade, to get back to your acquisition work force issue, do you think we should consider removing the entire acquisition work force from the current civil service system and placing it under an alternative system that would be more closely tailored to the needs of defense acquisition process?

Dr. **Wade**. I do not know the answer to that, Mr. Chairman. I certainly do not want to take a step to reach our common goal which will make it impossible to do.

We have this matter under study. The Packard Commission gives it a very, very high priority, our staffs are working together on this matter at this time.

How we go about it, I think remains for some time in the future.

I think also the bottom line in this regard might entail some perturbations on what I would call how we manage the process. How we go about putting the people force together will also have a bearing on that. That gets into the question of centralized procurement.

Certainly some more direction toward centralization from the Department, in my personal opinion, is required because it does address the issue of improvement and jointness in the planning, requirements, specifications, performance, acquisition and training. I think our technology and our moneys available actually demand we go this route.

Senator **Quayle**. Go in the direction of more centralization?

Dr. **Wade**. More centralization.

Senator **Quayle**. In other words, you think it would be worthwhile for us to consider it as an option alternative system?

Dr. **Wade**. Yes; my approach is that we ought to put all the facts in front of us and what the options are. We should not be afraid of them because we need to fix this problem.

In my opinion, the people force is one of the keys to fixing our long-term problem.

Senator **Quayle**. Do you think it would be a useful exercise for this subcommittee to entertain on a substantive basis consideration of alternative systems?

Dr. **Wade**. Yes, sir.

Senator **Quayle**. To the civil service work force?

Dr. **Wade**. I would say you demand my office to continue our work, look at the models, interact with you and your staff and come back and report.

Senator **Quayle**. I would like to get as much information about some of these alternative systems as you have. We, obviously, are in close contact and communications with the Packard Commission as well.

They are up against somewhat of a time situation and they have to adhere to that deadline. I do not know how they are going to make it. Maybe they will get an extension or reprieve.

Dr. **Wade**. My judgment is that they are fully at work on this one issue. If they make a judgment that this is the right direction to move, that recommendation is worth its weight in gold.

Senator **Quayle**. On the work force you have talked about time and time again the need for flexibility. I started to get into it, but you did not want to make program managers technocrats, you want to have them use creative energies to be managers.

I am wondering, as we look at what the trends in the past have been, legislation, regulation, things of that sort if we have not gone perhaps on the route of giving the individual not more flexibility, but less flexibility.

Is that a correct assessment?

Dr. **Wade**. Yes, sir.

Senator **Quayle**. Do you see the trends?

Dr. **Wade**. If we continue down the trends of trying to fix this problem at the margin directing solutions to micro issues, limiting a manager's flexibility, we will cause great difficulty in our ability to manage programs.

Many of the areas have been worked at the margin such as by requiring warranties. If you fix the process up front, going out and getting good equipment, that when it comes out works well, then you minimize your interest in the warranty.

Again, that is a symptom of the problem rather than a solution to the problem.

Senator **Quayle**. I think it would be helpful if you could detail for us with some degree of specificity some of the impediments that are presently placed upon your managers, particularly program managers, that take away some of their discretion and some of their flexibility. It is not necessary that you indicate we ought to repeal anything because you have said that you are not calling for any legislative repeal, but I would be interested in your view of policy and I would include in your response the regulations and things within the Department that you feel impede this idea of flexibility that you and I support.

If you can get that to us, it would be helpful.

Dr. WADE. Yes, sir, I look forward to that.

[The information follows:]

IMPEDIMENTS PLACED UPON MANAGERS

In recent years it has become increasingly difficult for program managers to maintain flexibility in light of the significant changes which have occurred in defense acquisition policy and the expanding role of Congress in defense acquisition through legislation. Taken individually, the policies and laws which have come into effect may each constitute a rational step toward achieving one or more objectives of the acquisition process. Taken as a whole, however, they constitute a considerable burden on a program manager which limits overall flexibility and discretion.

Recent legislation has required evaluation and reporting procedures which add to the administrative burden and contribute to lengthening the acquisition process. The Conference Report of the FY 1986 Authorization Act, for example, requires that the Secretary of Defense prepare and report an acquisition strategy for a program prior to the beginning of full-scale development. Revisions to acquisition strategy must also be reported and may not be implemented until 60 days after the report is received by Congress. Although acquisition strategy is already reviewed as a matter of course through departmental internal management, the new congressional requirement introduces another level of review creating an additional element for consideration and may result in a significant increase in acquisition time.

In addition, the FY 1986 Authorization Act also requires that, unless a specific waiver is requested and granted by Congress, competitive sources must be available for all major systems and subsystems from the period beginning with full-scale development through the end of production. In many cases, it does not make economic sense to establish a second source. Whereas formerly, the decision concerning second sourcing could be implemented once made, now the program manager is required to prepare and brief information concerning second scourcing through the chain of command and subsequently to Congress. Similar requirements now exist through legislation regarding warranties, independent cost analyses, and operational test and evaluation results.

Relaxation or elimination of these provisions would greatly reduce the administrative burdens placed on our program managers and would return to them the flexibility needed to more effectively manage their programs and to ensure the purchase of the best equipment at the lowest price.

Senator QUAYLE. A final question I have.

Assuming that we want to be helpful, to use your words, to streamline, do better, focus on new direction, I guess as we try to do this, my inclinations are to sort of look at the picture in a bigger sense than what we have done in the past.

When I say look at the situation in a broader perspective, I am talking about perhaps major reorganization, options or alternatives, that is a macro approach to procurement rather than the micro nit-picking type of approach that we have conducted in the past.

In listening to you today, I think that you would probably support our entertainment of some ideas in the macro arena and that we ought to at least consider some alternatives or some new models for the way we do our procurement business.

I am not talking about just increasing competition by 5 percent or trying to figure out whether you have to have five people on a qualified bidders list.

I am talking about a grander scale, something that we can examine.

Furthermore, I think we are at a time where we have a chance to really take hold of this and say, OK, there have been problems that have been reported, there have been some distortions, but some problems have not been distorted.

There are erroneous perceptions out there, we would like to clear up some of the perceptions. Now is the time to focus on this, work with the Packard Commission, with you, and with others to see how we can approach it on a grand scale and move to other models or systems than we have today.

I think you agree we ought to move in that direction to see what is out there to explore and probe and ask questions about this type of thing.

Am I correct about that?

Dr. WADE. Yes, sir, Mr. Chairman.

I would offer the point that our process has been working reasonably well to date. We have been turning out good equipment for the force. We need to turn out better equipment.

I think it is in that context we should approach this problem. The United States has the finest technology in the world and our research program should be made to assure that it's even better in the future, in the context of making sure we do our job better in the future. On the other hand, we should not just tear the system up and say in effect that it is broken, which I disagree with. If we do this, then I think we are approaching it in the right way.

At the same time we also have to make sure what we do can be accomplished rather than attempt to look at some problem in a grand sense that you might still be talking about 5 years from now and you have not accomplished anything.

I think we have to be careful. I think in that context I would support it rather than try to move into areas we might still be talking 5 years from now without any solutions in sight.

Senator QUAYLE. Senator Warner has joined us.

Senator WARNER. Thank you, Mr. Chairman.

I have known Mr. Wade for many, many years. I have always enjoyed our professional and working relationship. We are pleased that you have offered to serve in this position.

Dr. WADE. Thank you.

Senator WARNER. One of the more controversial issues in the implementation of the CICA has been the treatment of firms which make unsolicited proposals. There have been allegations that DOD takes innovative and unique ideas developed by these firms and uses them as a basis for solicitation.

My question: Has the Department of Defense used flexibility provided in CICA to adequately protect these innovative concepts?

Dr. WADE. We have had some discussion on this before, Senator Warner. I think the process is sufficient to protect such firms and their innovative concepts.

We still have to make sure that the right to creative research is protected and assure that scientists and engineers, particularly in a small firm, can see if they give us ideas, we will not open them up to somebody else without just compensation and mutual agreement.

This is a matter that will require serious attention at the top level, but at the same time I believe the process is there for a good manager to do his job.

Senator WARNER. Let us look at the small R&D firm.

How do you view the long-term impact of CICA on these small firms?

Such firms seem to believe the lack of protection under this proposal has a particularly deleterious effect on them.

Dr. **WADE**. I would like to hear more from the small firms and get specific details. I do not believe that to be true.

As I said before, I think there is a potential concern here. However, competition has been proven, I think, to be a valuable tool, a necessary tool, by the Department to get maximum utilization for its defense dollars.

I fully support and will make sure that my people support unsolicited research proposals and the protection of such proposals from unwarranted disclosure. That is the heart of our creative thinking. Any action that would denegrate that, I think we have to come down on and come down on hard.

Senator **WARNER**. We have a lot of reorganization people in the field now, so I would like to ask you the question.

Do you feel as Assistant Secretary of Defense for Acquisition and Logistics you have sufficient authority to force common acquisition policies on the services?

Dr. **WADE**. The answer to that, Senator, is yes and no.

My job is to be the senior staff official to the Secretary of Defense and he has direct command over the various services.

At the same time I think we are seeing instances where an individual service will get out in front and take an action that has a bearing on the Department as a whole. In this context it is bad action. We need to change that.

If a team works well together, you do not have these kinds of problems. I think overall there is a need for some further centralization for managing the overall operation.

Senator **WARNER**. Have you made those views known to our distinguished chairman.

Dr. **WADE**. Yes, sir.

Senator **WARNER**. And we can expect action because he is a man of action.

Dr. **WADE**. You can expect action from me.

Senator **WARNER**. Recently your office took exception to a Navy policy with respect to expenses for travel. The Navy has taken the position the contractor should only be reimbursed for travel costs up to the current Government rate.

What is the status of your discussions with the Navy?

Dr. **WADE**. The Navy was told that was a deviation from established policy and to cease and desist.

They are now in the process of asking for authority to deviate. I think that is still in process.

I think this is another example where strong initiative from one service is looked forward to, but when it has impact on the Department as a whole we frown on it. In this instance, we frown on that particular activity.

Senator **QUAYLE**. Thank you very much, Senator Warner.

Dr. Wade, thank you for your testimony. We do look forward to working with you.

There will be questions that will be submitted for the record. We look forward to having a good relationship.

Thank you.

Dr. **Wade**. Thank you, Mr. Chairman.

[Questions submitted to be answered for the record follow:]

Questions Submitted by Senator Dan Quayle

WARRANTIES

Senator **Quayle**. How is the cost/benefit analysis for warranties being conducted?

Dr. **Wade**. A cost analysis is being performed in every application of warranties. The specific tailoring of the warranty clause and the complexity of the application governs the task of performing a cost analysis. A factor that enters into this question is the absence of any previous data to analyze the full effect of our warranty implementation. We have no data base and it will be 5 years or more before a credible base will be available that can effectively be used in our cost analysis of warranties. As a result, very simple comparative analyses and estimating techniques are being used. The services are working the cost analysis issue and several contractor efforts are underway to assist in developing suitable approaches to further improve our cost analysis of warranties.

Senator **Quayle**. The warranty provision contained in P.L. 98-525 allowed for waivers in those cases in which it would not be cost effective to require a warranty on a system or piece of equipment. We included this authority to provide flexibility to the Secretary of Defense. This authority has not been used to date. Have any of the services requested OSD waiver authority for any system or equipment warranties?

Dr. **Wade**. To date there has only been one waiver which involved Army communication equipment used on several different types of helicopters. This waiver was done under the FY84 law and was requested in the interest of national defense because the timing of compliance with the FY84 warranty law would have disrupted production of the affected helicopter programs. The absence of waivers is not worrisome to the department. It simply illustrates that we are able to obtain cost effective warranties within the flexible limits provided by the FY85 law. Although the waiver does provide the Secretary flexibility, there are other flexible features of the provision contained in P.L. 98-525 that were not included in the FY84 law which lessen the need for waivers. Our policy still remains one of obtaining cost-effective warranties as prescribed by law. The specific features of the FY85 law compared to the FY84 warranty law which provide greater felxibility in our implementation are: tailoring warranty coverage to the specific weapon system; allowing the essential performance characteristics to be selected individually on each program; selecting the duration of time for warranty coverage; and the allowance for limiting a contractor's liability. These features when properly used in a given warranty have contributed greatly to our successful implementation of P.L. 98-525 and have so far made it unnecessary to use waivers.

CICA—GAO BID PROTEST

Senator **Quayle**. What has been the impact of the GAO bid protest provision on the ability of the Department of Defense and the services to procure items in a timely manner?

Dr. **Wade**. The CICA established two forums for bid protest procedures; the General Accounting Office (GAO) and the General Services Board of Contract Appeals (GSBCA). The latter is on a 3-year test basis for contracts involving nonmission critical ADP equipment. The GAO can hear these as well as other contract protests.

GAO has been in the protest resolution chain for some time. We welcome their advice is such cases. Generally, this outside review has indicated we acted properly. We understand from testimony given during hearings on H.R. 5184 of the 98th Congress that the low rate of rulings against the Department was one of the justifications for instituting more rigorous protest procedures. Our "success rate" is not expected to change much under CICA. However, the institution of the "22 cent injunction" has helped delay some contracts. That means that any disgruntled offeror for the price of a stamp can cause mischief.

As an example, within the Air Force, the number of protests increased 20 percent from fiscal year 1984 to fiscal year 1985 but the number of protests sustained stayed at 3.8 percent moving from 11 in fiscal year 1984 to 13 in fiscal year 1985. CICA was in effect for almost nine months of fiscal year 1985. This additional workload has detracted from doing other pressing tasks. We expect it to get worse.

The post-award stay provision is particularly troublesome. Our costs have increased as we have tried to implement this in good faith. In one case, a contract was protested within 10 days after award for the third time by the same protestor. The GAO had denied the two previous identical protests and denied this protest. However, the cost of the delay has been estimated at an additional $300,000 to restart this contract and put us back to where we were before. Both the contractor and the protestor are small businesses. Within DLA, 21 of 36 post-award protests involved small purchases of less than $25,000.

CICA—STREAMLINING ACQUISITION PROCESS

Senator **QUAYLE**. Is the concept of streamlining the acquisition process through the use of streamlining advocates compatible with the concept of simultaneously trying to increase competition through the competition advocates?

Dr. **WADE**. We see these efforts as complementary. The streamlining advocates are working to eliminate unnecessary specification requirements. This effort is expected to enable more contractors to participate in competitive source selections, thus enhancing competitive opportunities.

TECHNICAL DATA

Senator **QUAYLE**. The recent publication of the proposed technical data regulations has raised questions about the current Department of Defense regulatory process. The Defense Acquisition Regulatory Council chose to make a major departure from the existing Federal Acquisition Regulations relating to technical data rights. Concerns have been expressed that public comments were solicited too late in the process. What are your views on this problem?

Mr. **WADE**. The Defense Acquisition Regulatory Council and the civilian Agency Acquisition Council attempted to draft uniform FAR coverage for technical data. As a matter of fact, the coverage on Validation of Restrictive Markings will be in the FAR. With respect to technical data, however, the needs of the DOD are so different from those of the civilian agencies that a uniform policy was not obtainable. In accordance with P.L. 98-525, the DOD unique coverage will be issued in the DOD FAR Supplement. As explained at the public meeting held by the DAR Council on October 1, 1985, the initial DOD coverage was written against the DFARS for clarity and the final rule would be conformed to FAR drafting conventions. Until the civilian agency coverage is finalized, it is not possible to determine how much of the civilian agency coverage will be usable by DOD.

The DAR Council published its proposed rule in the Federal Register on September 10, 1985, and provided a 30-day public comment period in accordance with P.L. 98-577. The Director of the DAR Council and the Deputy Assistant Secretary of Defense for procurement met with industry representatives September 13, 1985, to discuss technical data. Due to the impact received on the proposed rule, the Council held a public meeting on October 1, 1985. Subsequently, an interim rule was issued to meet the statutory implementation date and the comment period of the proposed rule was extended by 90 days.

REGULATORY PROCESS

Senator **QUAYLE**. Can the regulatory system be structured in such a way that the public has an earlier opportunity to influence implementing regulations and yet provide for the timely implementation of legislation?

Mr. **WADE**. Under the provisions of P.L. 98-577, the Small Business and Federal Procurement Competition Enhancement Act, the Defense Acquisition Regulatory Council and the Civil Agency Acquisition Council obtain public comment on proposed regulations. Such comment is normally obtained and considered prior to issuing a new or changed regulation. However, a number of recent regulations had to be issued without prior public comment due to statutorily imposed implementation dates. In addition, the DAR Council works the public into the regulatory development process by holding periodic public meetings that include general discussion of pending cases. Also, when appropriate, the private sector is requested to provide early comments on proposed cases. We believe that these steps provide the basis for private sector participation in our regulatory development process.

COMMERCIAL PRICING

Senator **QUAYLE**. The proposed regulations on commercial pricing have been similarly controversial. In your view, what method should be used to determine "lowest commercial price?"

Dr. **Wade**. The Defense Acquisition Regulatory Council had to issue the revised regulations as an interim rule due to the statutory implementation date. During the subsequent public comment process, industry provided their views as to the definition of "lowest commercial price." The industry definition would have eliminated numerous categories of sales of commercial items from comparison without clear evidence that the government would not be entitled to that price. The Department of Defense believes that contractors should have to certify that the government is being offered the lowest price for its appropriate class of customer when adequate price competition is not present. In this situation, the contractor is in possession of superior knowledge as to sales of its commercial products. The DAR Council is providing a mechanism in its revised final rule for contractors to demonstrate in specific cases that certain classes of sales are inappropriate for comparison. This is felt to be a reasonable approach and allows the contracting officer to make a decision based upon specific facts.

ACQUISITION WORK FORCE

Senator **Quayle**. How much have current Civil Service restrictions affected your ability to recruit and retain a professional acquisition work force?

Dr. **Wade**. Civil Service restrictions, in my opinion, do not allow DOD to recruit and retain a professional acquisition work force. I am currently formulating ideas which I hope to review with OPM and implement to enhance the acquisition work force. I will also work with the Senate Armed Services Committee and the Packard Commission to develop a better system of retaining and recruiting such a work force.

My initial areas of concern include the Civil Service restriction not allowing DOD to require college degrees for acquisition personnel, except for engineers and lawyers; roadblocks to training and testing requirements as prerequisites for advancement to higher levels of responsibility; greater flexibility to transfer and remove people performing inadequately on their job; establishing higher salary levels for a professional Defense Acquisition Corps; and recruiting employees based on qualifications of the individual rather than qualifications of the vacant position. (This system, used successfully in the Foreign Service, is called "Rank in Person.")

QUALITY AS A CONCERN

Senator **Quayle**. You mention quality as being at the top of your agenda for the future. We seem to be developing an attitude which places a premium on the lowest cost for everything we buy. In your view, how can we structure the acquisition process to compete quality on an equal level with price and provide the Congress with a mechanism for understanding the wisdom of decisions based on quality rather than lowest price?

Dr. **Wade**. The concept of "competition for excellence" instead of "competition for price" is not a new concept. It has been successfully implemented in Japan and has now been adopted by the auto industry in America. For years the American auto makers have demanded the lowest prices, but in their quest for higher quality, they have demanded higher quality and lower prices. In return, they have replaced the usual 1-year contract with multi-year contracts to the suppliers who can meet their requirements.

In order to test this concept, we will need to have the data to justify awarding contracts for other than the lowest price. Therefore, we will probably select an electronic component to be the test commodity, since we will possess the test capability and data necessary for this experiment.

It is envisioned that for this test, and electronic part will be centrally procured for DOD and the defense industry to create a large enough market to be able to award multi-year buys to "excellent" suppliers. This will also incentivize suppliers to make investments for manufacturing and productivity improvement. The results of this experiment would be used for expansion/modification of this concept as well as justification of the concept to Congress.

In a related action, the DOD Directive 4105.62 on source selection was recently revised (September 9, 1985) to include quality as a criterion for source selection.

APPLICABILITY OF NEW LEGISLATION

Senator **Quayle**. Dr. Wade, most of the recently enacted legislation was conceived with the idea of the procurement of goods, as opposed to services in mind. Technical services, however, make up as much as 20 percent of the DOD procurement budget.

Could you provide some general insights into the application of competition provisions to service contracts?

Dr. **Wade**. The policy and procedural changes we have made, as well as the implementation of legislation, apply equally to the procurement of services as well as hardware. In fiscal year 1984, we awarded $7.5 billion in contracts for services. Of this amount, $5.5 billion was awarded for professional, technical and management services. Approximately 70 percent of the dollars for services in fiscal year 1984 were awarded competitively. We have no evidence that there is a problem that needs attention.

BREAKOUT OF SERVICE SUPPORT CONTRACTS

Senator **Quayle**. Have breakout specialists, for example, been directed to review service support contracts for potential breakout?

Dr. **Wade**. The requirements of the legislation and implementing regulations concerning the increase of competitive procurement apply to service contracts (including support contracts) as well as contracts for supplies.

There is increased emphasis on achieving competitive procurement at every level and the authority and responsibility of the competition advocates is aggressively directed at service support contracts. The nature of these types of contracts does not lend itself to establishing positions or a special structure for breakout specialists in the same manner as has been done with respect to replenishment spare parts. Review of the potential for breakout for service support contracts is the responsibility of the project office, the contracting office, and the competition advocate associated with the service.

FUEL PURCHASE CRITERIA

Senator **Quayle**. Explain your solicitation pricing and award criteria for the purchase of fuel through DFSC. Also, please explain when you make a conscious decision to go small business, why doesn't small business compete only against other small business?

Dr. **Wade**. Bulk fuel requirements are solicited by the Defense Fuel Supply Center (DFSC) for all requiring activities in a broad geographical area.

Bidders may offer prices on an origin basis (that is, the price at the refinery, with the Government responsible for delivering the product to the end user); destination basis (the contractor delivers to the end user); or both origin and destination (one price offered for origin, and an alternative price for destination). In destination bids, the bidder includes his transportation cost in the bid. For evaluating origin bids, the Government adds in its transportation cost to determine the "laid down" (that is, destination) cost of the bid.

Offers are evaluated to determine the award pattern which results in the lowest laid-down cost to the Government for the entire requirement being solicited. Determining the least-cost award pattern requires evaluating the laid-down cost of each origin offer to each destination. This involves a complex evaluation process because of the large number of destinations. The recent "Inland-West Coast" solicitation, for example, involved 170 destinations. Evaluation is further complicated by the fact that no bidder can offer an infinite amount of product. One origin bid might be the lowest offer for each of ten locations, but might be limited to a quantity sufficient for only one location. We must then determine which location to award to the low bidder, to result in the lowest cost for all locations. The second-low bid at each location may also have quantity limitations which present the same problem as the low bid. We use a computer model to compute the cost of every possible award pattern, and then select the award pattern which results in the lowest total laid-down cost to the Government.

Concerning the second part of the question, small businesses "compete only against other small businesses" in total small business set-asides. The Federal Acquisition Regulation (FAR) requires that, to make a total set-aside, the contracting officer must have a reasonable expectation that offers will be obtained from at least two responsible small business concerns, and that awards will be made at reasonable prices (FAR 19.502-2). We do not have a reasonable expectation of fair and reasonable prices if the small business sources do not have sufficient capacity to compete for the requirement. For example, if we need to buy 10 million gallons of fuel, and there are two potential small business sources who can each supply five million gallons, we would not have competition. Each company would really be a sole source, which could charge like any monopolist for its five-million gallon share. This is typical in bulk fuel. For example, in the most recent Inland/West Coast buy, we needed 1.6 billion gallons of JP-4 jet fuel, but small businesses offered a total of only about half a billion gallons.

While a total set-aside is precluded in such a situation, FAR does authorize a partial set-aside. The partial set-aside overcomes the problem of insufficient competition by requiring that "the set-aside portion will be awarded at the highest unit price(s) in the contract(s) for the non-set-aside portion" (FAR 52.219-7). The partial set-aside procedure for bulk fuel has been modified to accommodate the complex bid evaluation process, but retains the principle that a partial set-aside price must meet a competitive price.

[Whereupon at 11:30 a.m., the subcommittee adjourned, subject to the call of the Chair.]

IMPLICATIONS OF THE 1984 DEFENSE PROCUREMENT LEGISLATION

TUESDAY, OCTOBER 29, 1985

U.S. Senate,
Committee on Armed Services,
Subcommittee on Defense Acquisition Policy,
Washington, DC.

The subcommittee met in open session, pursuant to notice, at 10:07 a.m., in room SD-628, Dirksen Senate Office Building, Senator Dan Quayle (chairman) presiding.

Present: Senators Quayle, Goldwater, Warner, Levin, Bingaman, Dixon, and Glenn.

Staff present: Alan R. Yuspeh, general counsel; Alan L. Chvotkin, counsel; Jonathan L. Etherton, professional staff member; and Marie Chaillet, staff assistant.

Also present: Gerald J. Smith, assistant to Senator Goldwater; Henry D. Sokolski and Bill Hunter, assistants to Senator Quayle; Alan Ptak, assistant to Senator Gramm; Edward McGaffigan, Jr., assistant to Senator Bingaman; Charles C. Smith, assistant to Senator Dixon; and Milton D. Beach, assistant to Senator Glenn.

Also present: Jeff Minsky, Government Affairs Committee, and Bill Montalto, Small Business Committee.

OPENING STATEMENT BY SENATOR DAN QUAYLE, CHAIRMAN

Senator **Quayle**. The subcommittee will come to order.

This morning the subcommittee continues its series of hearings reviewing the status of the implementation of the 1984 defense procurement legislation. We have invited the Joint Logistics Commanders from the Armed Services and the Defense Logistics Agency to report on their experience with the legislation and the problems that they foresee.

The Joint Logistics Commanders testifying before the subcommittee today have a unique perspective on the defense acquisition process and the recent legislative changes that have been enacted. As the heads of the major Department of Defense buying commands, they have the responsibility for coordinating the procurement of virtually everything purchased by the Department of Defense.

The Joint Logistics Commanders also bring to the subcommittee the experience of many years of close involvement with the defense acquisition process.

Today we seek the benefit of personal as well as formal organizational views. The witnesses have not been invited this morning merely to serve as mouthpieces of the organization that each represents. We also expect to receive candid, personal observations, even if such observations may be at odds with official DOD policy statements. I expect and I know each of these witnesses will be able to give their personal opinion from a candid and objective viewpoint.

Before the witnesses begin their presentation, I would like to announce some changes.

The hearing scheduled for November 5 with the witness from the Strategic Defense Initiative Office has been indefinitely postponed.

Because of the great amount of interest, we have decided to make the November 7 hearing available for additional outside witnesses.

The witnesses this morning are:

Gen. Lawrence A. Skantze, Commander, Air Force Systems Command.

Gen. Richard H. Thompson, Commander, Army Materiel Command.

Gen. Earl T. O'Loughlin, Commander, Air Force Logistics Command.

Vice Adm. Thomas J. Hughes, Deputy Chief of Naval Operations (Logistics).

Lt. Gen. Donald M. Babers, Director, Defense Logistic Agency.

Welcome, gentlemen. Again, we will put your entire testimony in the record. We are looking for heart-to-heart discussions. You are the ones on the firing line.

If we need to make corrective steps, we need to know that. If you think we should keep going in the same direction, we need to know that. If there should be a change, we should sit down and have a meeting of minds and have a heart-to-heart discussion.

Senator Levin?

Senator **Levin**. All I want to say in an opening statement is that I want to commend you, Senator Quayle, for convening these hearings. Once again, you are initiating a set of hearings into a critical area about which we all have major concerns.

We want to make sure we not only act where we can act hopefully, but we correct any mistakes we make in the process. Congress will make mistakes as indeed the military will make mistakes in an effort to improve our system of procurement. We are not immune from that.

We are responding to a public outcry which is understandable. We want to make sure that their response is a constructive one and leads to efficiencies and not to the inefficiencies, paperwork and red tape.

We need your help in that process and to help us understand how what we have done works. We have taken a lot of steps in the last few years. I am delighted that our chairman has us together this morning so that we can hear from your firsthand knowledge of how these reforms are working in practice.

Senator **Quayle**. Senator Bingaman?

Senator **Bingaman**. I do not have a statement. I am looking forward to the testimony.

Thank you.

Senator **Quayle**. The prepared statement of Senator Dixon will be inserted in the hearing record at this point.

[The prepared statement of Senator Dixon follows:]

Prepared Statement by Senator Alan J. Dixon

Mr. Chairman, I am pleased that you have begun hearings on the Defense Acquisition Policy Subcommittee on the effect of the defense procurement reform legislation passed in the previous Congress. As a sponsor of the two major bills passed last year. I look forward to hearings from today's witnesses, who are the senior uniformed procurement officials of the military services.

The testimony I have read so far is somewhat distressing to me. I find that the services seem to be taking the position that certain parts of the Small Business and Federal Procurement Competition Enhancement Act of 1984 and the Defense Procurement Reform Act of 1984 are not workable, even though the legislation is just now being implemented. I found the prepared testimony very anti-small business. I find it hard to understand why competition is going to make the procurement system too complicated. There is a fallacy in the argument that developing subcontracting plans for contracts of $500,000 or more will not increase competition when we are making decisions on major weapon systems.

Mr. Chairman, the legislation we are discussing today has just recently passed Congress. Based on the testimony I have reviewed from today's witnesses, I think it is fair to predict that we will be having many oversight hearings on the way the military services intend to implement the laws that were passed in the 98th Congress.

Senator **QUAYLE**. General Skantze, welcome back.

STATEMENT OF GEN. LAWRENCE SKANTZE, U.S. AIR FORCE, COMMANDER, AIR FORCE SYSTEMS COMMAND

General **SKANTZE**. Thank you, Mr. Chairman.

I have submitted a statement for the record. I will make some brief remarks in opening.

I am pleased to have the opportunity to appear today to assess the status and the impact of the implementation of recent defense procurement legislation and the state of systems acquisitions within our Air Force Systems Command.

My overall assessment of the state of systems acquisition can best be described as turbulent. Today I would like to focus on how we can minimize the effect of that turbulence and highlight some of the initiatives we have taken in the areas of realistic budgeting and program stability.

I will also recommand to you actual steps which we must take if we are to achieve an efficient and effective procurement system mandated by the Competition in Contracting Act.

Realistic budgeting for a program is essential to establishing program credibility at all management levels and facilitating the tough decisions that must be made at key points during the development stage of the program. We have for some time instituted a system of independent cost analysis to challenge program estimates of major milestones or program reviews to encourage the realism that results from an independent review and enhance the credibility of our cost estimates.

The MK-15 identification friend or foe system, which is important to the United States and NATO, provides an excellent example of how the independent cost analysis process has been proven to be highly effective. The ICA process forces us to firmly identify, for the first time, exactly what we wanted that program to accomplish for us and also provide the Air Force budget position on the program which was sustained by the air staff.

During my 25-year career in systems acquisition I have seen the budgeting process grow from a requirement which occupied about a third of the time of a small group of individuals to an all-consuming effort involving all of the headquarters staffs and Air Force Systems Command and Air Force.

The emphasis on the budget is understandable to an extent, but this time could be much more productively used. It is time for Congress to reexamine what it is costing to prepare, defend and change the budget numerous times during the life of a program, not to mention the never ending "what if" effect exercises.

Realistic budgets are important to sound program management, but a realistic budget will be seriously undermined if the program does not remain stable. Program stability with emphasis on technical and fiscal stability is accomplished through a program baselining process which we try to maintain.

The best program manager simply has an extremely difficult time in living with constantly changing budgets and baselines. We are establishing the baselining process within the Air Force where the using command, the developing command and the logistics command sign up to exactly what is in the program in terms of technical content and cost and once that is agreed to and signed off, it cannot be changed without major four star commitment.

We have 15 major Air Force programs that have been baselined at Air Force vice chief level, including the C-5, B-1B, F-15, F-16, DSCS III and the Peacekeeper.

A commitment by Congress to stability is also required in order to assure program stability. Funding stability is vital. With funding stability we can man for development and production without stretchout, cancellations and restarts and, more importantly, we can be held responsible.

I strongly recommend that once Congress concurs with the program, they support that concurrence with the funds necessary to pursue the program in an efficient and cost-effective manner.

One way of assuring this would be the implementation of the 2-year budget. This would lend significant stability to the Air Force as well as all the services' programs and the contractors who execute them.

Multiyear contracting in AFSC alone has resulted in savings approaching $3 billion. The use of multiyear contracting, however, is significantly inhibited by the arduous review, approval, and validation process.

For example, on the B-1B program we did not obtain approval in time to include lot three of the offensive avionics with Boeing in that multiyear buy. Our savings were substantial, but could have been even greater had lot three been included. We ought to streamline the congressional multiyear requirements process.

It is all too easy to get wrapped up in the techniques to accomplish the development and production of systems and forget that without a professional work force, we cannot achieve an efficient and effective procurement system mandated by the Competition in Contracting Act.

One of our primary acquisition initiatives must always be the hiring, training, and retraining of highly qualified personnel. The decline in the relative attractiveness of civil service pay and benefits and the constant adverse publicity are having a negative effect, particularly in the high cost areas where we try to compete for people.

Frankly, our people are deathly afraid of making mistakes. In order to assure themselves they do not make mistakes, they ask for more data from the contractor to the point where nothing is at risk and this simply extends the procurement process even further.

In order to ensure we fulfill the mandate of CICA for an efficient and effective procurement system, we need your help in getting highly qualified college graduates into the contracting work force. I strongly recommend that Congress direct OPM to establish, as a minimum, the system contracting specialty as a professional series.

It is incongruous to me to go through all the grief we have over the last couple of years about how we contract and do procurement and still not be capable of making contracting a professional career.

Another area of concern is the stream of legislation which we have been implementing within the last couple of years and which we will probably be implementing in the future. We must remember that enacting a law or issuance of a policy is only the start of the process.

The more important part of the process is assurance that law or policy is effectively institutionalized which is a time-consuming process involving changes in the Federal acquisition regulations, the DOD regulations, in my case the Air Force regulations, and supplements to those regulations to be sure that the lowest levels of the institution, the people who are executing the program, understand what is desired to be implemented.

We estimate that this institutionalization process takes 3 to 5 years. I strongly urge a halt to new legislation impacting the acquisition process so that we can all get a better handle on the impact of the recent legislation and more knowledgeably recommend where we should go from here.

Some of the legislation currently being considered is of particular concern and I will now briefly discuss some of the issues confronting us at this time.

Competition has been a subject of intense congressional interest for many years and was certainly the impetus behind the Competition in Contracting Act. Legislative proposals would require the Secretary of Defense to establish both an annual competitive dollar goal and report on our efforts to expand competition.

This is a good example of not giving an initiative time to become institutionalized prior to establishing new requirements.

The Competition in Contracting Act has been in place since April 1, 1985, a relatively short time. Let us give that program a chance before we add still more requirements with respect to competition.

I am, personally, very proud of the job Air Force Systems Command has done in the area of competition; 26 percent of AFSC's dollars were competed in 1984 and this dramatically increased to 36 percent in 1985.

We must be careful, however, that we do not go overboard in competing products and services and disincentivize contractors from making long overdue capital investments. You simply cannot have both. To incentivize the contractor to spend his money on plant and equipment, he has to see at least a reasonable time to get a return on his investment.

We must strike a balance particularly in view of the industrial modernization improvement programs and the tech mod funds which have been zeroed out in the 1986 HAC markup. It is essential that these funds be reinstated to continue our facility modernization currently on contract with 90 contractors with a potential for program savings in excess of $3 billion.

Dual sourcing is an excellent technique for reducing program risks and production costs in selected situations. But it is not the panacea that current legislative proposals would lead one to believe. It can double the cost of development efforts and reduce production rates even below the rates we are now experiencing.

You cannot do the B-1B's, C-5B's, or F-15's by dual source. But be assured I am a strong supporter of dual sourcing when there is reasonable assurance that large production quantities or high technical risk indicates that we will reduce the overall cost as a result.

Within AFSC we have a number of dual source programs that are working very well, such as the imaging infrared Maverick and combined effects munitions which we started several years ago.

Requirements to notify Congress or obtain congressional approval prior to taking or not taking certain actions inevitably extend the acquisition leadtime. For example, on a recent Joint Stars competitive contract award we were delayed at least in part by a requirement to notify Congress that we would not be dual sourcing prior to entering into contract for full-scale development. Delays such as this drive up costs and divert us from our main goal.

However, one situation where new legislation is certainly required is in the area of the Freedom of Information Act—FOIA—which has wreaked havoc in the area of procurement. In fiscal year 1984 we spent 14.4 man-years of effort responding to requests at a cost of $515,000.

Further, the basic tenets of competitive source selection are threatened by FOIA abuses. For example, we recently awarded a competitive contract for the survivable collective protection system which is a defensive chemical shelter. Since the award, we have received six different FOIA requests for the winner's total proposal, all the offeror's unit prices and all source selection inquiries and responses.

We must edit the six volumes line by line. The winning contractor is extremely concerned about the compromise of his competitive advantage.

We need an amendment to FOIA to exempt commercial information in its entirety.

I have already described the state of systems acquisitions as turbulent and recommended a number of steps to reduce that turbulence. However, this subcommittee represents the most important step that must be taken because I believe it is critical that a single focal point be established for defense procurement legislation.

Today no centralized congressional oversight and review takes place to eliminate inconsistencies and conflicts between various legislative packages. Over the last 2 years there has been an avalanche of piecemeal procurement laws that has created havoc within the acquisition process.

For example, synopsis requirements changed significantly between Public Law 98-72, CICA and Public Law 98-577. Further, there has been over 1,000-percent increase since 1970 in congressionally requested studies and reports and another 1,000-percent increase in other mandated actions for DOD.

Finally, a number of provisions were aided to the fiscal year 1986 appropriations bill which could substantially impact the procurement process. Such legislation is difficult. We must create a coherent, structured and consolidated legislative process for defense procurement issues.

It is essential that both the Senate and the House work together to establish the most efficient and effective acquisition system possible.

In conclusion, I believe we must join together to improve our effectiveness, maintain the highest standards of integrity and never lose sight of the critical importance of the job we do. The acquisition process is not an easy one. It is increasingly frustrating.

Lest we forget, the acquisition process is also critical to our Nation and its ability to effectively defend itself. Should we fail to meet our challenges, we fail not only ourselves, but our Nation. We must not and cannot accept such a consequence.

This completes my statement, Mr. Chairman.

[The prepared statement of General Skantze follows:]

PREPARED STATEMENT OF GEN. LAWRENCE A. SKANTZE, COMMANDER, AIR FORCE SYSTEMS COMMAND, U.S. AIR FORCE

I am pleased to appear before you today to assess the status and the impact of the implementation of recent defense procurement legislation and the state of systems acquisition within Air Force Systems Command [AFSC]. My overall assessment of the state of systems acquisition can best be described as "turbulent." Today, I would like to focus on some of the key initiatives we are pursuing in AFSC to minimize the effects of that turbulence and recommend to you additional steps which we must take if we are to achieve an efficient and effective procurement system mandated by CICA. By efficient and effective, I mean a system that allows DOD to acquire the products and services it needs in the most timely, economical, and efficient manner.

Before addressing these initiatives, I want to explain the scope of AFSC's mission. Our job is to acquire the capabilities needed by the operational commands to deter war and, if necessary, to win, if deterrence fails. The command is responsible for the research, development, test, evaluation, and acquisition of fully supported weapons systems. Last year, AFSC obligated approximately $32.3 billion and managed 13,700 Active Air Force contracts whose face value was in excess of $109 billion. The 11 systems command divisions and centers are responsible for the acquisition of all major Air Force weapons systems, including missiles; armament; aircraft; engines; radar systems; and command, control and communications systems. Moreover, we are also responsible for the very important task of advancing the technology base for future systems. Our Contract Management Division performs contract administration surveillance at 30 operating locations, involving 17 major defense contractors, and has responsibility for contract administration at 6 major contractor corporate offices.

To provide a framework for my comments, I would like to briefly review with you a study which was conducted at AFSC several years ago. This study, commonly referred to as "The A^3 Study" for "Affordable Acquisition Approach," compared systems developed and fielded in the fifties and sixties with those of the seventies and eighties and addressed the question: "Does the development of major systems take longer and cost more?" To no one's surprise the resounding answer was "yes." For example, in constant dollars, the cost of air superiority fighters increased thirteenfold; light weight fighters, threefold; and fighter bombers, fourfold. All other types of systems increased in cost with the sole exception of radar early warning systems. Production rates increased for air-to-ground weapons, air-to-air missiles, and medium range missiles; but production rates for the big ticket items—fighters, ICBM's, bombers, and cargo aircraft-dropped significantly. The causes of the cost growth and delays raised some eyebrows. The study identified 14 factors which adversely affected both the recent and earlier programs but four factors stand out not only because they occur in over half of the recent programs, but also because their rate of occurrence is up markedly from the pre-1970 programs. These factors are funding instability, technical complexity, external management impacts, and multiple program interfaces. As a result of the A^3 study and the defense acquisition improvement program, we have taken a number of meaningful steps to reduce program cost and the time it takes to field new systems.

With that study in mind, I would like to concentrate on some of the initiatives we have undertaken in the areas of realistic budgeting, program stability, economic production rates, and multiyear procurement and discuss the progress we have made. I will also make recommendations as to how we can jointly maximize the benefits of these initiatives. I will also share with you my views on two key aspects of the acquisition process which are frequently overlooked: The acquisition work force and the institutionalization of change.

Realistic budgeting is the first major initiative I want to address. Realistic budgeting for a program is essential to establishing program credibility at all management levels and facilitizing the tough decisions that must be made at key points during the development stage of a program. Program personnel are imbued with the optimism and enthusiasm that are crucial to program execution but that same optimism can sometimes lead to unrealistic budget projections. To temper that enthusiasm, we have instituted a system of independent cost analyses [ICA] to challenge program estimates at major milestones or program reviews. The purpose of an ICA is not to discredit program estimates but, rather, to encourage the realism that results from an independent review and enhance the credibility of the estimates. The Mark XV identification friend or foe system provides an excellent example of how the independent cost analysis process has been proven to be highly effective. The ICA process forced us to firmly identify, for the first time, exactly what we wanted that program to accomplish for us. Not only did we develop program definition as a result of the ICA, but the results of the review also provided Air Force budget position on the program which was sustained by the air staff.

Closely related to ICA's and an essential ingredient to the development of realistic service budgets are independent cost estimates. To improve cost estimating, we have increased the authorized manning, improved our training and education process, and undertaken modest, but high-payoff research into cost estimating of technology areas, such as software, advanced composite materials, and advanced electronic circuitry. These initiatives have enhanced our ability to ensure we have a good cost estimate to support the full-scale development and production approval process and the DOD initiative to budget to most likely cost. While we have not achieved all of our desired cost estimating improvements, we have made significant progress, as evidenced by the fact that costs on our 32 programs covered by the selected acquisition report [SAR] have remained relatively stable over the last 2 years.

During my 25-year career in systems acquisitions, I have seen the budgeting process grow from a requirement which occupied about a third of the time of a small group of individuals to an all consuming effort involving all of the headquarters staffs at AFSC and Hq USAF. The emphasis on the budget is understandable to an extent, but this time could be much more productively used to focus in on our programs and ensure that our contractors deliver quality products, within cost, and on time to meet critical IOC dates. It is time for Congress to reexamine what it is costing to prepare, defend, and change the budget numerous times during the life of the program, not to mention the never-ending "what if" exercises.

Realistic budgets are important to sound program management, but a realistic budget will be seriously undermined if the program does not remain stable. Our second initiative, therefore, is program stability, with emphasis on technical stability. Given the state-of-the-art technology with which we deal on a regular basis, the temptation to enhance a weapon system's capability can be irresistible. Baselining is the technique we use to maximize technical stability. A program baseline is a formal, written agreement between the users, program mangers and the Air Force which states the specific requirements to be satisfied, provides a clear definition of the program to meet these requirements, and lays out resources to be allocated for the effort. When these three elements are consistent, the baseline is approved by the Air Force Vice Chief or Assistant Vice Chief [AF/CV/CVA] and forms an agreement whereby Hq USAF agrees to support the necessary resources and all affected commands within the Air Force promise to deliver the system on time and within cost. Changes to this approved baseline must be ratified at the same level as the original baseline.

AFSC is committed to a total baselining posture. Fifteen major Air Force programs have been baselined at the AF/CV/CVA level, including the C-5, B-1B, F-15, F-16, DSCS III, and Peacekeeper to mention a few. These baselines have enhanced across-the-board understanding of program content, effectively stopped program requirements growth, and detailed program financial constraints. We are continuing to aggressively pursue baselining at this level and such programs as the North Warning System, Lantirn, C-17, and DSP are currently in process. In addition, 40 programs are being baselined at the Majcom Deputy Chief of Staff level. Finally, all remaining programs are being considered for baselining at the product division level.

Although baselining entails a pact between the air staff, AFSC, and the other affected commands, a commitment by Congress is also required. In order to assure program stability, funding stability is a necessity. With funding stability, we can plan for development and production without stretchouts, cancellations, restarts, and "what if" exercises. Recognizing the difficult task facing all of us in light of the fact that we have a 2-year Congress, a 4-year President and a 10-year program, we must all work together to achieve program and funding stability. I strongly recommend that once Congress concurs with a program, they support that concurrence with the funds necessary to pursue the program in an efficient and cost-effective manner. One way of assuring this would be the implementation of a 2-year budget. This would lend significant stability to the Air Force as well as all of the other services' programs and the contractors who support it. Further, it would help us in achieving our third initiative, which is economic production rates.

The A^3 study showed definitely that stretchouts of development and production schedules are commonplace. We have initiated efforts to identify and fund economic production rates and it is probably the biggest single cost reduction vehicle available to us. If a contractor underutilizes production capacity, we must still pay for many of the costs associated with that unused capacity since it is unavailable for other purposes. If we fully utilize the contractor's capacity, we can lower our unit costs to a minimum and that is the objective we should all be striving for. For example, the Titan 34-D average unit cost increased by $15.5M per missile when the build rate decreased from 5 to 2 missiles. Results in this area continue to be mixed, at best. Recent congressional action on the fiscal year 1986 President's budget, the F-15, F-16, Maverick, GBU-15, and combined effects munitions were among programs which were stretched. However, the good news was that the AIM-9 Sidewinder, AGM-130, and TR-1/PLSS were all accelerated. If we are to minimize production costs, the Air Force, DOD, and Congress must all be firmly committed to establishing and supporting economic production rates.

If economic production rates are supported, we can increase the savings even more through the use of multiyear contracts on selected programs. Multiyear contracts engender the most efficient use of contractor and subcontractor resources because they have a longer term commitment from the Air Force and are more willing to make investments in efficient production facilities. Further, purchasing can be done on a larger quantity basis, resulting in a still lower cost per unit.

Although multiyear contracting in AFSC alone has resulted in savings approaching $3 billion, we can do more. The use of multiyear contracting, however, is significantly inhibited by the arduous review, approval, and validation processes. For example, on the offensive avionics buy from Boeing for the B-1B, we requested authority to contract on a multiyear basis for production lots III, IV, and V. By the time Congress approved the request, it was too late to include lot III in the multiyear buy. Our savings were substantial but could have been even greater had lot III been included.

The multiyear approval process should be a consequence of the normal budget process and not an addition to it. Once the Congress authorizes the multiyear approach in an appropriations bill, it should not revisit the decision. For example, Congress should not have to see savings validation data unless validated savings are significantly less than anticipated. In general, Congress is too deeply immersed in the details of multiyear acquisitions. This adds paperwork, leadtime, and administrative complexity to the jobs of the contracting officers and program managers trying to plan, negotiate, and execute multiyear contracts. The appropriations and Armed Services Committees need to consolidate the scattered direction and guidance on multiyear submissions that have appeared in committee reports since 1982. In so doing, it would be a great service to the agencies if the requirements that fuel micromanagement were removed.

A different type of inhibitor of multiyear contracting is the fiscal year 1985 appropriations bill requirement that the economic order quantity portion of multiyear contracts be funded to termination liability. The HAC bill for fiscal year 1986 would continue this requirements. It nullifies the flexibility provided in the permanent law on multiyear procurement (10 U.S.C. 2306(H)(5)), contrary to the original congressional intent. Agencies cannot choose among funding alternatives, selecting the one that makes the most sense in the circumstances. Instead, they must tie up millions of dollars worth of total obligation authority to cover a contingent liability.

AFSC has never terminated or cancelled a multiyear contract and the risk of our ever doing so is extremely low. It is counterproductive to lock up large amounts of TOA to cover such "termination liability" when that TOA could be used to obtain some useful product. Congress should delete this requirement from section 8037 of the fiscal year 1986 appropriations bill.

In general, the appropriations bill should not be used to make temporary amendments to permanent law. Since multiyear authority was established in 1982 in 10 U.S.C. 2306, every appropriations bill has changed its terms for purposes of the particular fiscal year covered by the bill. "Stability of law" would be a welcome addition to the multiyear environment.

These are certainly not all of the initiatives we have ongoing within AFSC. We are also actively pursuing other areas such as should cost analysis, support and readiness issues, reliability and maintainability, and production base analysis as means of fielding better systems more economically in the future.

It is all too easy to get wrapped up in the techniques to accomplish the development and production of systems and forget that without a professional work force we cannot achieve the efficient and effective procurement system mandated by CICA. It is essential that one of our primary acquisition initiatives must always be the hiring, training, and retaining of highly qualified personnel. Our civilian retention rates are currently within acceptable limits on a macro basis, but the decline in relative attractiveness of civil service pay and benefits, and constant negative publicity are having an effect particularly in high cost areas such as the Los Angeles area where industry provides salary and benefit packages which we cannot match. Training has been a problem, but the Air Force, and specifically AFSC, has been aggressively reducing the backlog of mandatory training courses for our contracting personnel. We are projecting that the December 1985 backlog of training quotas will be less than one half of the 5,542 quotas we had in December 1983. My major concern regarding contracting personnel is OPM's intransigence regarding the stature of contracting personnel. Several years ago, there was a concerted effort to reduce the grade structure in contracting—exactly the opposite approach we need. Fortunately, that effort failed. It is important to note that E.O. 12352, signed in March 1982, on Federal procurement reform directed OPM to consult with the heads of executive agencies and ensure that personnel policies and classificiation standards meet the needs of executive agencies for a professional procurement work force. Unfortunately, OPM has not initiated any activity to support this direction in the Executive order. We firmly support Secretary Taft's recent efforts to enhance professionalism of our procurement work force. We understand, however, that OPM essentially turned down his request for assistance on this matter. But we need help getting highly qualified college graduates into the contracting work force. I strongly recommend, therefore, that Congress direct OPM to establish, as a minimum, the system contracting specialty as a professional series. This would enable us to recruit and select more highly qualified individuals with college degrees at entry level positions and ensure we fulfill the mandate of CICA for an efficient and effective procurement system.

Another area of concern is the stream of legislation which we have been implementing within the last couple of years and which we will probably be implementing in the future. I am frustrated at times, as I am sure you are, with the length of time required to see the results of legislative or executive initiatives. The fact of the matter is, however, that enacting a law or issuance of a policy is only the state of the process. The more important part of the process is assurance that the law, or policy, is effectively institutionalized which is very time-consuming. In addition to incorporating the requirement into applicable directives, extensive training must be conducted and our working level personnel must fully understand the requirement before we can expect to see the results of the initiatives. With the flood of complex legislation we have been implementing (such as the Competition in Contracting Act, warranty requirements, and now data requirements), we seem to be in a constant state of turmoil interpreting new requirements, writing regulations, training our people, and verifying implementation. We have not had time to examine the results of the new requirements, refine our policies, and then develop recommended changes we believe are appropriate. Changes to a system must be done in a deliberate and methodical fashion which includes the following steps: Understanding the system and what it must do; understanding how the sytstem actually works; identifying problems as they arise; getting top management to support long term solutions; and applying enough of the best people to do the job of institutionalizing the solutions. Recent reforms have done little or nothing to alleviate the cost and schedule drivers I spoke of earlier and are in fact exacerbating our leadtime problems. We need the opportunity to and I strongly urge a halt to new legislation impacting the acquisition process so that we can all get a better handle on the impact of recent legislation and more knowledgeably recommend where we should go from here.

I would be remiss if I were to discuss the institutionalization of reforms and not emphasize the important role that the DAR Council and Civilian Agency Acquisition Council play in implementing reforms. The FAR system is the link between the laws of Congress and the contracting officer who negotiates, for example, a contract for missiles or space parts. The quality of the FAR and its supplements is therefore of vital importance to Congress (which wants to ensure its laws are implemented) and the contracting officers (who need to be sure they are complying with all applicable laws). If the FAR is unclear or out of date, it fails both Congress and the contracting officers.

We all share responsibility for making the FAR system work. It is our only mechnism for maintaining a systematic acquisition process. It puts all the changes in context. Whether they result from initiatives or edicts, the changes must take hold there if they are even to become routine at the working level—in other words, "institutionalized."

I am not satisfied with the existing regulatory system. The FAR was to be a Federal-wide acquisition regulation—it has succeeded only modestly in achieving that goal. This is in part the fault of Congress which passes legislation applicable only to DOD or legislation for the defense and civilian sectors that is only "similar," requiring implementation to be accomplished separately for the Defense Department and civilian agencies.

Every effort should be made to consolidate the acquisition regulations into the FAR, particularly for those things that have plant-wide impact on contractors. The supplements to the FAR should be truly implementing guidance as opposed to raising totally new policy areas.

The FAR systems needs work. It needs resources from all agencies dedicated to its proper maintenance and improvement. And those writing it need well thought-out, statesmanlike comments from those of us who use the FAR. We need to give these tasks the priority they deserve.

Some of the legislation currently being considered is of particular concern and I will now briefly discuss some of the issues confronting us at this time.

Competition has been a subject of intense congressional interest for many years and was certainly the impetus behind the Competition in Contracting Act. Current legislative proposals would require the Secretary of Defense to establish annual dollar goals for the award of competitive procurement and report to Congress annually on promoting and expanding competition. This is a good example of not giving an initiative time to become institutionalized prior to establishing a new requirement. The Competition in Contracting Act formalized the Competition Advocate Program and that has been in place since 1 April 1985—a relatively short time. Let's give that program a chance before we add still more requirements with respect to competition. I am personally very proud of the job AFSC has done in the area of competition. Twenty-six percent of our dollars were competed in 1984 and we are projecting an increase to 31 percent or more in 1985. Based on our current initiatives and a decrease in follow-on procurement, we are projecting an increase to about 45 percent in fiscal year 1987. Additional reporting requirements will hinder rather than assist our on-going efforts.

Dual sourcing is an excellent technique for reducing program risk and production costs in selected situations, but it is not the panacea that current legislative proposals would lead one to believe. It can, of course, double the cost of development efforts and reduce production rates even below the rates we are now experiencing. I am a strong supporter of dual sourcing when there is reasonable assurance that large production quantities or high technical risk indicate that we will reduce overall cost as a result; but it does not make sense as an across-the-board acquisition strategy. Another aspect of the dual sourcing legislation that concerns me is the requirement to submit a report describing the acquisition strategy to Congress.

The management of the programs should be left to the services once the decision is made to fund it, and Congress should not be involved in the management of programs at that level. Requirements to notify Congress or obtain congressional approval prior to taking or not taking certain actions inevitably extend the acquisition leadtime even if a specific congressional response is not required. For example, on a recent joint stars contract award we were delayed at least in part by a requirement to notify Congress that we would not be dual sourcing prior to entering into a contract for full-scale development. Dual sourcing was clearly not possible in this program. Clearly, these approval or notification requirements are manpower intensive and time-consuming efforts that rarely, if ever, result in a change to our approach.

Spare parts pricing is also receiving a lot of attention in proposed legislation based on the premise that spare parts prices have been unreasonably high. That premise is incorrect. There are a handful of cases where we have paid too much for an item out of the millions of items bought by DOD. These cases warrant the extra attention we are now paying to spare parts but do not warrant a plethora of legislative reforms.

One situation where new legislation is certainly required is in the area of the Freedom of Information Act [FOIA]. Although I cannot speak to the merits of the act in other aspects of Government, I can say that it has wreaked havoc in the area of procurement. The Department of Justice recently expanded its interpretation of the term "records" under FOIA to include technical data and other valuable property which substantially increases the number of DOD documents subject to FOIA. Several areas concern me. The first is the amount of resources to respond to FOIA requests. In fiscal year 1984, we spent 14.4 manyears of effort responding to requests at a cost of $515K. Reimbursement was only in the amount of $26K. More serious is the threat of FOIA requests to the procurement process. Requests for competition sensitive and commercial information are detrimental to the procurement process because they discourage contractors from giving us all of the information we need in the acquisition process. Further, the release of engineering drawings and technical manuals, which are frequently the target of requests, has the potential to technically level contractors in subsequent competitions. The basic tenants of competitive source selection are threatened by FOIA abuses. For example, we recently awarded the contract for the survivable collective protection system [SCPS]—A full and open competition for a potential $1 billion program. Since the award, we have received six different FOIA requests, including requests for the winner's total proposal, all offerors' unit prices, and all source selection inquiries and responses—an unbelievable level of detail. Because of the current legal interpretation, we cannot deny a request in total under the commercial exemption. Instead, we must edit the six volumes line-by-line. The winning contractor is extremely concerned about the compromise of his competitive advantage and has agreed to edit the proposal. His schedule is already tight, and this diverts his attention from contract performance. We need an amendment to FOIA to exempt commercial information in their entirety.

In conclusion, I believe it is fair to state that the acquisition community is in a state of turbulence and trauma. Our most important job is to keep our people motivated and committed to our acquisition process during such troubled times. This is no easy task when we are surrounded by the clamor of negative press, a constantly changing legislative and regulatory environment and a need for continuous training due to the plethora of changes. As leaders we must join together to improve our effectiveness, maintain the highest standards of integrity and never lose sight of the critical importance of the job we do. The acquisition process is not an easy one. At times it is frustrating, frequently it is confusing and often it is difficult. Lest we forget, the acquisition process is also critical to our Nation and its ability to effectively defend itself. Should we fail to meet our challenges, we fail not only ourselves, but our Nation. We must not and cannot accept such a consequence.

This completes my statement. I look forward to discussing the areas referenced in your letter announcing this hearing.

Senator QUAYLE. Thank you.

Our next witness is Gen. Richard Thompson, Commander, Army Materiel Command.

STATEMENT OF GEN. RICHARD THOMPSON, U.S. ARMY, COMMANDER, ARMY MATERIEL COMMAND

General THOMPSON. Mr. Chairman, members of the Senate Armed Services Subcommittee on Defense Acquisition, I am Gen. Richard H. Thompson, Commander, U.S. Army Materiel Command.

I appreciate this opportunity to provide my views on the implementation and impact of the 1984 procurement legislation contained in the Public Law 98-369, the Competition in Contracting

Act [CICA]; Public Law 98-525, the Defense Procurement Reform Act of 1984 [DPRA]; and Public Law 98-577, the Small Business and Federal Procurement Competition Enhancement Act of 1984.

The intent of the recently passed legislation is good and has the Army's full support. Our ultimate objectives must always be to ensure the best buys for the taxpayers' dollars, and to demonstrate that we are responsible stewards of the public trust.

I have submitted a formal statement for the record and with your permission, I would like to summarize that statement now.

Senator QUAYLE. Please do.

General THOMPSON. We are committed to competition, price reasonableness, quality products, contractor responsibility, and quality procurement in general. In fact, many of the areas in these statutes address initiatives already taken or planned by the Army Materiel Command as a result of our internal spare parts reviews.

On the negative side, however, the promulgation of multiple statutory reforms over a short period has impacted the acquisition process in terms of both extended leadtimes and decreased productivity. We must not lose sight of the fact that our system is people dependent and people intense.

Seemingly minor changes in structure and policy can in due course cause major disruptions at our operating levels. Let me highlight some of our concerns with specific legislation you requested be addressed.

Regarding Public Law 98-369, CICA, the legislative creation of a competition advocate organization to independently review exceptions to competition is beneficial.

However, the statutory approval requirements established for less than full and open competition have added complexity and leadtime to the procurement process as did the requirement for technical and requirement certification.

Also of concern is the emphasis on full and open competition as opposed to adequate and effective competition. Full and open competition does not always result in lower prices.

There is a break-even point where the addition of competitors to a given acquisition may no longer result in improved prices and where the addition of potential competitors may serve only to exacerbate administrative delays and increase cost.

The CICA revised protest procedures which may require work to be stopped on contracts already awarded is a matter of concern. This provision has potential for abuse by unsuccessful bidders and can result in substantial penalties in terms of delay and disruption cost.

Moreover, the CICA authorized use of the General Services Board of Contract Appeals to resolve protests is inappropriate and places extraordinary demands on our system.

The ability to maintain a proper balance over the long term between obtaining the latest state of the art technology and the acquisition data rights required for future competition may be compounded with the implementation of Public Law 98-525.

Two issues contained in Public Law 98-577 of concern to the Army are related to Small Business Administration Procurement Center Breakout Representatives and removal of the exemption of small purchases from the certificate of competency process.

The Small Business Administrative Procurement Center Breakout Representative duplicate functions and responsibilities already being performed by existing personnel. Removal of the exemption of small purchases from the certificate of competency process will result in increased leadtime and costs to accomplish the affected small purchase actions.

As a related matter, inconsistency between requirements to synopsize at $10,000 and the simplified purchase threshold of $25,000 further reduces our flexibility to purchase low value items in a relatively noncomplex, quick turnaround fashion.

Let me emphasize that on balance the recent legislative changes have had both positive and negative impacts. At a recent meeting I held with my key contract officers, the people on the firing line, there was unanimous agreement that the loss of productivity, confusion, and complexity are the overriding issues associated with the procurement reforms of the last 2 years.

Time is needed to institutionalize the changes made to date. It is only in a less volatile environment that we can concentrate on and measure the benefits of the changes made to date. Then, if necessary, we can identify those additional actions which are needed to further improve the process or modify any actions already taken which, in fact, are not resulting in the benefits expected to be obtained.

Thank you, sir.

[The prepared statement of General Thompson follows:]

PREPARED STATEMENT OF GEN. RICHARD H. THOMPSON, U.S. ARMY

Mr. Chairman, members of the Senate Armed Services Subcommittee on Defense Acquisition Policy. I am General Richard H. Thompson, Commander, U.S. Army Materiel Command.

I appreciate this opportunity to provide my views on the implementation and impact of the 1984 procurement legislation contained in the P.L. 98-369 the Competition in Contracting Act [CICA]; P.L. 98-525, the Defense Procurement Reform Act of 1984 [DPRA]; and P.L. 98-577, the Small Business and Federal Procurement Competition Enhancement Act of 1984.

The intent of recently passed legislation is good and has the Army's full support. Our ultimate objectives must always be to ensure the best buys for the taxpayers dollars, and to demonstrate that we are responsible stewards of the public trust.

We are committed to competition, price reasonableness, quality products, contractor responsibility, and quality procurement in general. In fact, many of the areas in these statutes address initiatives already taken or planned by the Army Materiel Command as a result of our internal spare parts reviews. In these cases, the legislation served to accelerate implementation of these initiatives and to raise the consciousness levels of our acquisition personnel and senior management.

On the negative side, promulgation of multiple statutory reforms over a short period impacts the acquisition process in terms of extended leadtimes and decreased productivity. This may ultimately result in degradation of our wholesale logistics capability which can translate directly into readiness. Consequently, we must not lose sight of the fact that our system is people dependent and people intense. Seemingly minor changes in statute and policy can, and do, cause major disruptions at the lower operating levels.

Concerning the specific legislation you requested be addressed: P.L. 98-369 [CICA], redirected the long-standing emphasis on procurement by formal advertising, to competition whether or not such competition is achieved through sealed bids or negotiations. This is considered a positive step long overdue. Legislating the creation of a competition advocate organization, to independently review exceptions to competition, is also viewed as beneficial. Competition advocates had previously been established at AMC's major subordinate commands as part of our spare parts initiatives and proved to be an effective check and balance on our procurement system which, unfortunately, is often clouded by conflicting priorities and objectives.

On the other hand, the statutory approvals established for less than "full and open" competition, particularly those requiring approval by management above the field level, have added complexity and leadtime to the procurement process, as did the requirement for technical and requirements certification.

We are concerned with the emphasis on "full and open" competition as opposed to "adequate and effective" competition. "Full and open competition" does not always result in lower prices. There is a break-even point where the addition of competitors to a given acquisition may no longer result in improved prices. The unconstrained addition of potential competitors may also serve to exacerbate administrative delays. And increase the cost to provide procurement packages to potential contractors, to verify sources qualifications, and conduct responsible source selection evaluations.

The CICA-revised protest procedures, which may require work to be stopped on contracts already awarded, is a matter of concern. This provision has a potential for abuse by unsuccessful bidders and can result in substantial penalty in terms of delay and disruption costs. This cost vulnerability is particularly true for contracts involving continuing services, contracts for products to be provided as government furnished materiel, and contracts for initial and follow-on logistics support.

Moreover, the CICA—authorized use of the General Services Board of Contract Appeals [GSBCA] to resolve protests is inappropriate. Board procedures are highly formal and place extraordinary demands on our technical, procurement, legal and administrative personnel.

P.L. 98-525 provided requirements in many areas similar to those included in our spares initiatives. Examples of these are the requirements for: competition planning; review of procurement history and item description; identification of actual source of supplies; economic order quantities; and, allocation of overhead to parts.

Although limited experience has been gained on the specific regulatory implementation in these areas, they are viewed as positive reinforcement. Also positive are the revisions to prior warranty requirements reflected in this legislation.

The ability to maintain a proper balance over the long term between obtaining the latest state of the art technology and the acquisition of data rights required for future competition may be compounded with the implementation of Public Law 98-525.

The revisions to pre-qualification standards have only recently been implemented. While no experience is available to date the implementing coverage appears to have overcome prior concerns relating to delays in award incident to post-opening qualification.

Two issues contained in P.L. 98-577 of concern to the Army are related to the Small Business Administration Procurement Center breakout representatives and removal of the exemption of small purchases from the certificate of competency process.

The SBA Procurement Center breakout representatives duplicate functions and responsibilities already being performed by existing small business representatives, our competition advocate organizations and our in-house breakout personnel. Not only does such layering result in administrative delays with no apparent value added, it also competes for constrained resources, specifically space and administrative support since these resources are currently being provided by DOD agencies as a part of overhead.

Secondly, removal of the exemption of small purchases from the certificate of competency process will result in increases in administrative leadtimes and the costs to accomplish the affected small purchase actions. Moreover, without this exemption, the cost to resolve the competency issue. In certain cases, will be more than the cost of the materiel being purchased.

As a related matter, the inconsistency between the requirement to synopsize at $10,000 and the simplified purchase threshold of $25,000 further reduces our flexibility to purchase low value items in a relatively non-complex, quick turn around fashion.

On balance, the recent legislative changes have had some positive and some negative impacts.

At a recent meeting I hosted for key contracting officers, there was unanimous agreement that "loss of productivity." Confusion, and complexity are the overriding issues associated with the procurement reforms of the past two years. To put their frustration in perspective, 11 changes to the far have been issued since its publication on 1 April 1984. Another 14 changes to the DFARS have been issued and 40 policy directives have been issued by the Department of the Army. While all were not directly related to legislation we are addressing here today, based on historical precedent, substantially more policy refinements are expected.

Time is needed to institutionalize the changes made to date. By this I mean to solidify interpretations, establish precedents, reeducate the acquisition workforce, stabilize the process and gain some long-term experience. It is only in a less volatile environment that we will be able to concentrate on, and measure the benefits of, the changes made to date. Then, if necessary, we can identify those additional actions which are needed to further improve the process or modify any actions already taken which, in fact, are not resulting in the benefits expected to be obtained.

Senator QUAYLE. Next, Gen. Earl T. O'Loughlin, U.S. Air Force, commander, Air Force Logistics Agency.

STATEMENT OF GEN. EARL. T. O'LOUGHLIN, U.S. AIR FORCE, COMMANDER, AIR FORCE LOGISTICS COMMAND

General O'LOUGHLIN. Thank you very much, Senator Quayle.

I appreciate the opportunity to participate in today's hearing on defense procurement reform legislation.

I have provided a prepared statement that I ask be placed in its entirety in the record.

Senator QUAYLE. It will be placed in the record.

General O'LOUGHLIN. In the full statement I explain in greater detail the nature of the Air Force Logistics Command's mission and how we are organized to get the job done. Because our objective today is to discuss some of the recently enacted legislation aimed at improving the Department of Defense procurement process, my opening remarks will concentrate on the effect of these laws on the Air Force Logistics Command.

AFLC is responsible for providing logistics support to meet Air Force readiness and sustainability objectives. Without the engines, fuel, munitions, spare parts, and maintenance we provide, our sophisticated systems would contribute little to national defense. We need to provide Air Force operators with quality goods and services, on time, at the right price.

The recent problems in spare parts pricing you are all familiar with resulted from what we call a decade of neglect. Decreasing manpower and inadequate funding led us to a poverty mindset in AFLC acquisition. Buying minimum quantities and concentrating almost exclusively on prices of high ticket items led inevitably to the well publicized horror cases.

In 1983, when we discovered these weaknesses, we completely reviewed our spares procurement system and identified 178 areas where we could improve. Except for a few areas that needed long-term solutions, we have made the improvements. We have worked to increase competition and we are beginning to see concrete savings and positive results.

We have changed our procedures to ensure that each item's price is realistic. We have reinforced the "zero overpricing" program. Most importantly, we have taken steps to overcome manpower shortages and upgrade our data systems. The net effect of all of this is to begin to break out of the poverty mindset in funding and in manpower.

The overall results are encouraging. In fiscal year 1984 we saw verifiable savings of $529 million and through three-fourths of fiscal year 1985, an additional $518 million.

However, the final results of our internal initiatives and reform legislation will not be clearly visible for quite a while. We will need more time for the corrective actions to have their full effect because we are making changes that must be institutionalized.

By institutionalizing, I mean interpreting and understanding the law, including it in applicable policies and regulations, and communicating this understanding throughout the organization until it becomes routine at the working level. With an organization as large as AFLC, such institutionalization does not happen quickly.

But the main point of my testimony is the positive and negative effects of recent laws. In my prepared text I discussed these concerns in detail. Now I would like to address the most important effects from each of the specific laws under review today.

The Competition in Contracting Act was the most significant piece of procurement legislation since 1947. It was designed to make major, positive reforms in the acquisition process and to a large degree it succeeded. The most positive effect is the emphasis on competition and away from "formal advertising." Our principal concerns with CICA are twofold:

The new stop work provisions on protests filed within 10 days of awarding a contract.

And the emphasis on "full and open" competition rather than on "adequate and effective" competition.

Historically, our command has lost only 1 percent of the protests filed against it. Having to stop work on 99 percent of protested awards where the GAO subsequently upholds the Air Force position significantly increases our leadtime and costs and could potentially erode readiness.

On the second issue, we believe adequate, effective competition, especially on small purchases, is a more sound business philosophy.

The Defense Procurement Reform Act of 1984 successfully resolved some inconsistencies in previous legislation. The changes in warranty legislation have helped us comply with congressional intent.

However, the law's other provisions negatively affect our buying process. In particular, the requirement to tell any potential bidder how to qualify as a vendor will be difficult, if not impossible, to implement. It also increases our vulnerability to substandard performance on critical safety of flight items.

Finally, concerning the Small Business and Federal Procurement Competition Enhancement Act of 1985, we see one major detriment, the requirement that the SBA is giving the option to issue a COC, eliminating the $10,000 threshold for small purchases.

This will mean longer leadtimes and require more manpower on what should be simplified small purchase procedures.

One additional note on Public Law 98-577. Breakout procurement center representatives totally duplicates our competition advocate and lengthens contract award leadtime.

The effect of acquisition reforms on Logistics Command has been a steady, significant increase in the length of time it takes our buying people to award contracts. The average award time for all buys increased from 54 days in May 1983 to a high of 133 days in April 1985.

This trend is serious because of what it does to operational field support and the money we will need to fill the leadtime gap in spares support. To maintain the same level of support, each day's gap requires around $11 million.

In my complete statement for the record, I made some specific recommendations regarding the three laws addressed today. These changes could improve the process and reduce administrative leadtime and costs without removing or disturbing the good the legislation accomplished.

I would like to address five basic themes that are essential to making permanent improvements. I believe they are equally important. The five objectives are:

First, decentralize authority, responsibility, and accountability. Approval authority on most matters should be delegated as much as possible and normally no higher than my two star center commanders. Followup audits and reviews can ensure compliance with the law and hold officers responsible and accountable for their actions.

Second, simplify the system and the processes. Reform should make the DOD procurement system easier to access, and simpler to manage. While some of the reforms have done this, the overall result is a system that is more complex.

Third, follow or adopt existing standard commercial practices whenever and wherever possible. To a layman, the Government appears to prefer inventing new bureaucratic processes.

Fourth, recognize the limits of competition. We must be careful not to pursue competition for its own sake. In fiscal year 1984, Logistics Command awarded 24 percent of its contract dollars through competitive methods. Although the final numbers are not yet available, we expect to realize around 31 percent for fiscal year 1985, and even higher numbers for fiscal year 1986.

However, competition has its limits. They are:

Technical limits, when the skill and expertise we need from a second source are not available.

Business limits, when the inside knowledge of, for instance, certain complex or capital intensive manufacturing process, does not exist outside the existing source. These would include small and midrange businesses for which this intellectual knowledge is the "company jewels."

Economic limits, when the time and money we need to establish additional sources are not available or justifiable.

My bottom line is this, we must decide to compete on a part-by-part basis. Our goal is to compete 100 percent of the time when it makes sense to compete, and zero percent of the time when it does not.

Finally, the fifth objective is that legislation should provide policy direction, not regulatory mandates. Any law that arbitrates an action, whether it levies percentages to be achieved, mandates precontractual reviews at very high levels, or requires any specific levels of accomplishment is not beneficial to us, the vendor, or the taxpayer.

Laws that require specific actions also rob our flexibility to ensure we can make proper business decisions and carefully maintain stewardship of the taxpayers' money.

Each year Logistics Command buys around 100,000 parts from an overall inventory of about 870,000. In any given day our buyers buy items ranging from a stainless steel bolt to a missile guidance system, and they try very hard to make sure we pay a reasonable price for each item.

Even if we make this process 99^{44}⁄$_{100}$-percent pure, we could still leave room for up to 600 horror cases. I know we are better than that, but I also know we are not perfect. Legislation cannot make this process 100-percent pure. The costs in time, money, and manpower for a perfect system are prohibitive.

Both the Office of Federal Procurement Policy and the DOD/IG took a look at what we have done since fiscal year 1983 to correct the system. Both found we had identified the contributing problems and had begun to solve them. Both recommended the defense procurement system be given time to fully institutionalize and evaluate the many initiatives already being taken before it had to cope with any more significant changes.

In summary, I want to emphasize that Air Force Logistics Command is fully committed to resolving the pricing concerns raised by Congress, the administration, and the American public. I think we have proven our commitment by the additional resources we have dedicated to these issues.

We will most certainly continue our search for new and better ways of getting our job done; but, we must always be careful not to undermine the reason we buy spare parts and that is Air Force readiness.

Mr. Chairman, that concludes my statement.

[The prepared statement of General O'Loughlin follows:]

PREPARED STATEMENT OF GEN. EARL T. O'LOUGHLIN, COMMANDER, AIR FORCE LOGISTICS COMMAND, U.S. AIR FORCE

Thank you very much, Senator Quayle. I appreciate the opportunity to participate in today's hearing on the defense procurement system. I would ask that my statement be inserted in the record in its entirety. In this statement I will address matters of prime concern to the Air Force Logistics Command--the Air Force organization most deeply involved in the purchasing of spare parts. These concerns parallel those expressed through the Joint Logistics Commanders initiatives which has come to be known as the Pendulum briefing.

Logistics in Perspective

First, our goal in AFLC is to put an operational, force-readiness focus on every aspect of our logistics business, and we are making significant strides in that direction.

Before focusing on spare parts procurement within the Air Force Logistics Command, it is essential that we all have a general perspective of the Air Force Logistics Command and its acquisition task.

Logistics is very big business, and because weaponry and equipment are becoming more complex, logistics workload is clearly increasing. On the other hand, the Command is primarily manned with a civilian work force that has declined dramatically over the years, essentially stabilizing after 1979 at around 80,000 people.

Besides its five (5) major Air Logistics Centers (ALC) at Sacramento, San Antonio, Ogden, Warner Robins, and Oklahoma City, along with specialized activities at Tucson, Arizona, Wright-Patterson AFB, and Newark, Ohio, AFLC also relies on contractor-operated depot facilities in Wichita, Kansas; Birmingham, Alabama; Lake City, Florida; and Greenville, Texas.

We also rely on many key oversea contractor facilities in Getafe, Spain; Manching, Germany; Brindisi, Italy; Gosselies and Liege, Belgium; and Kim Hae, Korea, to provide logistics support to operational units in their area--thereby decreasing pipelines and increasing readiness. And we've gained a new capability at RAF Kemble in the United Kingdom.

All these facilities would do us little good without the skilled people to man them or administer their operations. In fact, in terms of manpower, AFLC, with almost 98,000 people, accounts for over 11% of the Air Force work force today.

One of every three of AFLC's civilians is a tradesman, craftsman, or laborer. They are also everything from clerical workers and managers, to scientists, engineers, and computer specialists. Perhaps more than any other command, AFLC represents a real cross-section of America's skill and talent.

Within the contracting community of AFLC, we have around 4000 people (95% civilian) issuing solicitations, conducting pricing reviews, negotiating terms and conditions of proposals, and finalizing contracts. Most of these people--4,000--are located at our five major Air Logistics Centers and they complete 108,000 buy actions for nearly $13 billion each year! As you can see, AFLC is primarily a high volume, low dollar business. When you add the top two dollar thresholds in Figure 1, only 12% of our contracts have a price of $100,000 or more, yet these contracts total 93% of the dollars we spend. On the other hand, the bottom two dollar thresholds account for only 7% of the dollars we spend but involve 88% of our contracts, which have an average price of less than $100,000. We cannot conclude from this brief analysis that the big dollar value contracts are important and the smaller ones are not. In fact, the smaller dollar value contracts are often most important in that they involve the delivery of spares to solve critical support problems.

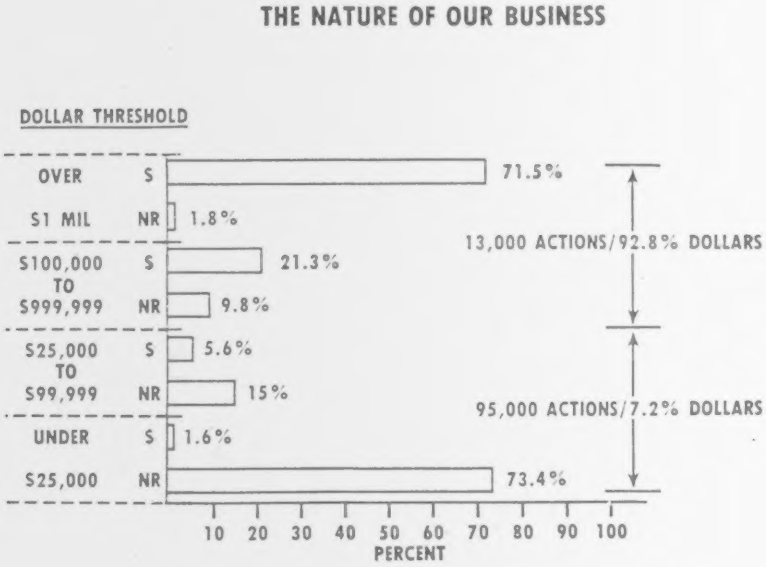


Figure 1

Spares

In the late seventies and early eighties, a series of major factors contributed to a decade of neglect in the acquisition of spare parts. For one thing, we continued to rely on automated management systems installed in the mid-sixties. For another, we had to accomplish an increasing workload without more people because of arbitrary budget process ceilings. Third, replenishment spare parts were severely underfunded from 1977 to 1982. And finally, we experienced--with the economy--high rates of inflation. All these factors led to the so called "horror stories."

What does this have to do with logistics? Our capacity to deter, or to fight and win, hinges on the ability to project fighting forces where and when they are needed and sustain them for as long as they are needed. Readiness and sustainability are the backbone of today's combat forces. Logistics involves determining the goods and services necessary to defend this nation, what resource investments must be made to do that, and then actually making those investments. When the required resources are not available, combat force readiness suffers. Scarce resources are not all that makes logistics the paramount military concern today, but also the kinds of resources required and the speed with which we must provide these resources.

For one thing, technology has made our weapon systems more complex to operate and more complex to support. Today, a front line weapon system requires war readiness supply kits with thousands of line items, prepositioned around the world, to meet multiple peacetime and wartime requirements. That system also requires high-technology, environmentally controlled maintenance facilities and large numbers of highly skilled people.

For another, technology has accelerated events. Where once warfare developed over months or years, conflicts can now reach full intensity in a matter of hours. Consequently, today we are approaching logistics in a real-world, operational way. Since the availability of spares is a key determinant of readiness and sustainability, their affordability has become a major concern as well.

A spare part can be anything from a noncritical fastener costing a few cents to a radar processor costing thousands of dollars. In purchasing roughly 100,000 replenishment parts each year, the Air Force Logistics Command spends about 70 percent of its spares procurement dollars on just 2 percent of these parts--closely controlled and audited big-ticket purchases. On the other hand, nearly all the media reports of overpricing have focused on the low-value, low-visibility spare parts--the nuts, bolts, and washers.

The word "spares," whether applied to low-cost or high-cost items, unfortunately suggests something unneeded or extra and distorts the pricing issue. Spares for military hardware are purchased not because they may be needed, but because they will be needed. In the case of technologically sophisticated weapon systems, Air Force people predict component failures. These predictions, in turn, serve as the basis for buying, stocking and distributing replacements--so-called "spare" parts.

Call for Reforms.

I am not here today to criticize any particular reform. I do want to emphasize, though, that a policy or statute is only the start of the process. More important is insuring that the policy or law is effectively institutionalized--that policy is being interpreted, understood, included in other applicable policies and regulations, and finally becomes a routine at the working level. Sometimes the time and effort required to complete this process is expensive and time-consuming, especially when many changes are made over an extended period--the situation over the past two years.

Buying Initiatives

Problems buying spare parts have generated several initiatives to improve the buying process. The Secretary of Defense's 10/25 Point Program and the Support Equipment Acquisition Review represent major administrative reforms. The Federal Acquisition Regulation (FAR) was also a significant milestone. For the first time, all government contracting was subject to the same rules and regulations. Although generally the FAR did not establish new rules and regulations for DOD, it did result in an easier-to-read and easier-to-use regulation. Although the FAR system, properly implemented, will help the people who actually do the work, it also required extensive training and reorientation of our people.

Additionally, the Defense Acquisition Improvement Program included general initiatives to improve the acquisition process, reduce weapon system cost, and make those systems more responsive. While primarily focused on major system acquisition, the program involved AFLC in the areas of multiyear procurement, economic production rates, improved support and readiness, and emphasis on increasing competition. The steps the Air Force is taking to control costs do not involve constraints and needless regulation but, rather, free competition.

Probably the greatest impact from the administrative reforms within recent years resulted from the Air Force Management Analysis Group on the acquisition of spare parts. Called the AFMAG, this select group of Air Force professionals, formed at the direction of the Secretary of the Air Force in May of 1983, performed a comprehensive study encompassing all the preceding separate reforms. AFMAG identified 178 recommendations to improve spare parts buying, 58 of which directly related to this command. AFLC has taken effective and aggressive actions to implement these recommendations that affect acquisition of initial spares, through the purchase and delivery of replenishment spares, to developing methods to ensure we can give production support to our weapon systems.

We in Logistics Command are also working closer than ever before with Systems Command to improve the initial provisioning of spares as well as to solve the problems of adequate reprocurement data and data rights up front during initial system acquisition.

We have improved how we buy replenishment spares by improving the requirements generation process, starting purchase requests earlier, buying economic order quantity items once a year, consolidating more for better and more efficient buying, and emphasizing multiyear contracting for spare parts.

Establishing competition advocate offices at each buying center focuses more attention on breakout and competition and also provides value reviews of unit prices to make sure we pay realistic prices.

We are also improving our major automation and management information systems which will have a significant positive impact on the process.

Increased manning and the positive motivation and training of the entire acquisition work force are also major initiatives we have undertaken.

However, FAR implementation, the Defense Acquisition Improvement Program, and the AFMAG-Study are certainly not the only reforms we have implemented in recent years. Now I want to turn to some of the major legislative reforms that we have recently implemented. I would like to point out that the legislation I will be discussing is very specific in nature. For the most part, current public laws are going well beyond the statement of general policy. Instead, they are also providing substantial regulatory guidance on the specifics of implementation.

Public Law 95-507

Passed in 1978, this law was one of the earliest attempts at reform and still affects the acquisition process. Its provisions required prime contractors to develop subcontracting plans and made us provide bid sets to any and all small businesses upon request.

Public Law 95-507 is intended to give the small business community a chance to bid on government contracts. AFLC fully supports and is a proven advocate of small business participation in the furnishing of goods and services we require. Over $1 billion in AFLC awards go to small businesses and we meet our goals. Although we believe that Public Law 95-507 has generally been effective, certain aspects of this law should be reconsidered in the interests of an efficient defense procurement system.

Specifically, the requirement to furnish bid sets to all small businesses who request them has increased costs and administrative lead times. We do not believe small business in general suffers by limiting, to a reasonable amount, the number of solicitations (bid sets) available for any given competitive purchase. In many situations, adequate competition already exists and additional bidders generally increase administrative costs but provide little or no offsetting cost reductions.

In many cases, the cost of providing bid sets for all small businesses who have requested them is excessive as compared to the total cost of the purchased parts. In short, Public Law 95-507 often forces us to spend more in total administrative costs than the amount of the purchase. Furthermore, on average, less than one-third of those who receive bid sets actually submit a bid. The impact on AFLC of providing unlimited bid sets is an increase in both cost and administrative lead time.

Considering these factors and recognizing that we are establishing effective and current bidders' mailing lists, we recommend that Title II, Chapter 3, Section 223, of Public Law 95-507 be repealed and/or changed so that contracting organizations may make a economically reasonable number of bid sets available to small businesses. We owe the taxpayers a cost-effective, small purchase procedure.

Another impact of Public Law 95-507 and the other laws we will be discussing is the increase in complexity they inevitably create. Each of these laws adds a degree of difficulty our negotiators, contracting officers, and staff must deal with in the course of buying Air Force goods and services.

Public Law 98-72

The intended purpose of Public Law 98-72 is to improve small business access to Federal procurement information and to promote competition. Most of the requirements of this law have now been superseded by those of Public Law 98-369, the Competition in Contracting Act (1 April 1984).

However, Public Law 98-72 did increase our administrative lead times and the workload associated with (1) processing to HQ AFLC sole source justifications over the applicable threshold, and (2) delays in the acquisition cycle occasioned by its mandatory waiting periods. One requirement of this law which was not superseded by Public Law 98-369 deals with the Freedom of Information Act and expands the ability of contractors to receive sensitive information relating to their competitors. The shortcoming of PL 98-72 is that it was based upon the concept that longer waiting periods and extra paperwork requirements would remove the real world impediments to competition.

Competition in Contracting Act (CICA)

The intended purpose of this legislation is to make contracting more effective and more business-like. While we fully support the focus on competition, we believe that especially for smaller dollar purchases, "adequate" and "effective" competition is a more sound business philosophy than full and open competition. Full and open competition drives you to the point where increasing competitors on a given purchase is counterproductive. After adequate and effective competition is achieved on low dollar value actions, cost is usually not reduced by adding more bidders. Also, those parts of this law requiring justification and approval to purchase under less than full and open competitive procedures increase lead times. The new protest procedures that require stopping work on ongoing contracts, potentially increasing their cost in many cases, and the still more cumbersome synopsis procedures have a significant impact on both lead time and administrative costs.

Don't misunderstand me. We like the tone of the CICA. We agree that the emphasis should be on achieving competition, not on the form or formality it takes for achieving "full and open" competition. Also, excluding the prime for competitive second sourcing purposes will both enhance competition and expand our industrial base in selected acquisitions. More detailed descriptions in the synopses have improved a contractor's ability to determine whether or not to request a copy of a solicitation. We also believe that the use of Justification and Approvals has increased competition because we now demand stronger justification for not competing items. However, the administrative burden of coordinating Justification and Approvals through the Small Business Administration, the Competition Advocate, the item manager and their technical and managerial reviews, and finally the procurement office is both costly to perform and control.

Public Law 98-525

The Defense Procurement Reform Act of 1984 (contained in the 1985 DOD Authorization Act), was intended to resolve some of the inconsistencies among the previous legislation and by and large did. For example, this bill incorporated into law the warranty changes to Public Law 98-94 negotiated between DOD and Congress following passage of that earlier legislation. Additionally, reverse engineering on items considered to be good candidates for breakout has increased, as has our ability to obtain rights to technical data. Contractors are also more readily identifying the actual manufacturers of items to Government buyers.

Requirements of this law, however, are also likely to affect our buying process. It requires DOD, down through the major command level, to publish major policies for comment before their implementation, which may result in better and more equitable policy but will no doubt inhibit our ability to promulgate timely policy.

DOD is in the process of implementing the new data requirements, and their effects on our PCOs and program managers are yet to be determined. On 10 September 1985, the proposed rules were published in the Federal Register. On 20 September 1985, interim rules were published, and final rules are still pending. The pre-qualification requirement promises to complicate the process of establishing qualified sources on critical performance, source restricted parts. While this provision may ultimately encourage competition and reduce procurement costs, adding the additional sources for certain products increases Government risks with product reliability and safety and ultimately risks in costs as well. In constructing a framework for qualifying additional sources and to lower these risks, our limited technical staff must assume the expertise of design engineering, manufacturing technology staffs, and testing agencies to identify detail requirements and concerns in the manufacturing, quality control, and testing areas. These concerns are amplified when changing sources of supply. These efforts recognize that the designing source is no longer the source of supply, that a learning curve in manufacturing an item must be reaccomplished when changing sources, and that processes and manufacturing techniques, as well as design, affect product reliability and safety.

Finally, this law's requirement to establish four-year tours for program managers is conceptually sound. While it has not affected us yet, we may well find that it limits the flexibility of our field commanders to best use their people.

Public Law 98-577

The last major piece of legislation to be addressed today is the Small Business and Federal Procurement Competition Enhancement Act of 1984. While perhaps appropriate to non-DOD elements of the Government, one part of this law simply and fully duplicates the AFLC Competition Advocate functions, and increases lead time without any hope for a return on that investment. The law did, however, reduce the synopsis period for research and development acquisitions from thirty to fifteen days. This change in the rules regarding synopsis of requirements is the third since the initial provisions, established by Public Law 98-72 on 1 October 1983. The requirement to solicit public comments on policy changes was extended to the total federal sector. Finally, the provision of this law that will affect this command most is that portion that establishes a requirement for referral of small business nonresponsibility determination to the Small Business Administration for a Certificate of Competency for small purchases below the $25,000 threshold. This requirement will likely result in many referrals for low dollar acquisitions. This is particularly significant to AFLC because three-fourths of our buy actions fall within the small purchases threshold.

Although no data is yet available, the end result will probably be longer to complete small purchases, with significant administrative cost and effort.

The combination of Executive and Legislative reforms coupled with our initiatives already in process have had a significant effect on the acquisition process--much of it positive. Some of the significant positive results we will discuss are the result of our earlier initiatives, while others are a direct outgrowth of the reforms I've just reviewed.

The Air Force is doing what is necessary to ensure the American taxpayer gets his money's worth from a credible military-industrial complex. We are aggressively identifying and resolving policy, procedural, and regulatory impediments that have historically blocked, interfered with, or otherwise encumbered our efforts to achieve fair and reasonable spare parts pricing. At this point, I'd like to highlight in more detail the initiatives we have taken and the successes we have experienced to date. I must first emphasize that the problems we've had in the past were not caused by poor performance by our working level people. They were doing a good job executing programs consistent with the existing resources and policies provided by management. Management's policies, procedures, and especially the lack of adequate manpower and dollars formed the primary cause of the problem.

Figure 2 represents the results of efforts we made to focus on the serious problems in our procurement system.

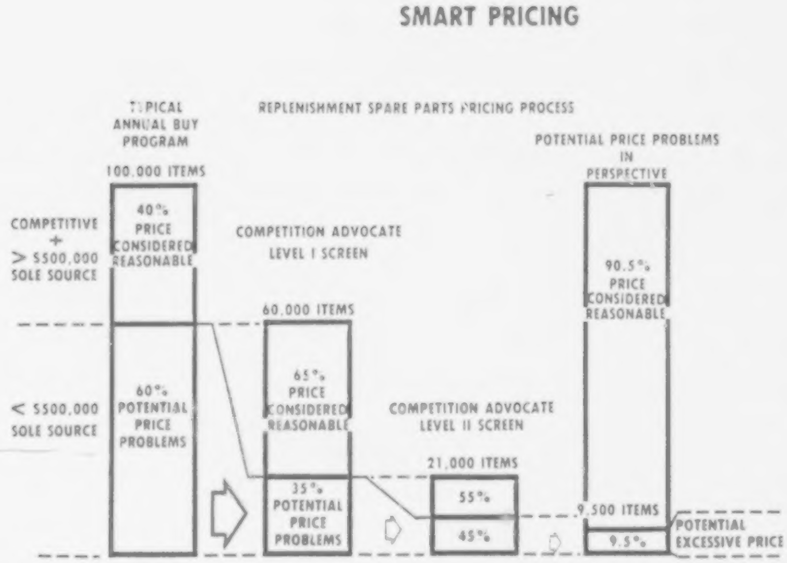

SMART PRICING
TYPICAL ANNUAL BUY PROGRAM
REPLENISHMENT SPARE PARTS PRICING PROCESS
POTENTIAL PRICE PROBLEMS IN PERSPECTIVE
100,000 ITEMS
COMPETITIVE + > $500,000 SOLE SOURCE
40% PRICE CONSIDERED REASONABLE
COMPETITION ADVOCATE LEVEL I SCREEN
60,000 ITEMS
90.5% PRICE CONSIDERED REASONABLE
< $500,000 SOLE SOURCE
60% POTENTIAL PRICE PROBLEMS
65% PRICE CONSIDERED REASONABLE
COMPETITION ADVOCATE LEVEL II SCREEN
21,000 ITEMS
35% POTENTIAL PRICE PROBLEMS
55%
45%
9,500 ITEMS
9.5%
POTENTIAL EXCESSIVE PRICE

Figure 2

Note that while we buy on the average over 100,000 different replenishment items each year, after deducting those items procured competitively or through the negotiation process involving detailed cost and pricing data, approximately 60,000 items are subjected to review by the Competition Advocate to determine whether or not past prices represent the intrinsic value of the items. In about 65% of the cases we find no apparent or potential price problem. The remaining 21,000 items are subjected to a more detailed estimated cost build-up where we find about 45% are still potentially overpriced. Viewed from the universe of 100,000 parts, less than 10% or about 9,500 of these items, fall in the category of potential pricing problems. The majority of the items are priced fairly, either through the market place by competition or through negotiation.

Nonetheless, the 10% target area represents a large enough problem to warrant actions to insure that the deficiencies of the past are not repeated. We have stepped up to that responsibility and while we cannot cover at this time all the various initiatives we are taking, we want to share some of the more significant ones.

AFLC Initiatives

Most importantly, we are correcting the inadequate and faulty policies and procedures, we have made the first installment toward providing adequate resources and we are seeing positive results in the form of concrete savings. I will highlight some initiatives and share some of our success stories.

The many recommendations for improvement addressed two major problem areas: the need for increased competition and improved pricing. My comments will address these areas, some of the AFMAG's more significant recommendations, the Air Force Logistics

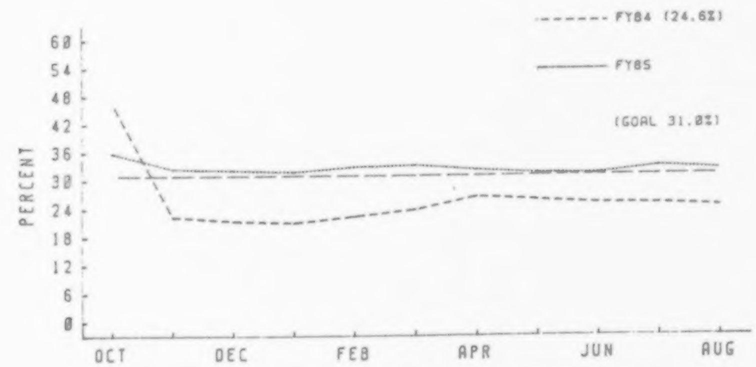
Command's initiatives and progress to date, and our prognosis of what lies ahead.

Competition and Breakout

AFLC has made a substantial commitment to increasing competition and breakout of previously sole sourced items to their actual manufacturer. We have allocated 1,480 manpower spaces to the Command Competition Advocate Program as evidence of that commitment. We believe it is paying off.

The dollars competitively awarded by this command have dramatically increased in Fiscal Year 85 over Fiscal Year 84. Each year we set a competition goal. For Fiscal Year 85, it was 31% (Figure 3). As you can see, Fiscal Year 85 is about seven percentage points better than Fiscal Year 84, a significant 30% increase.

CUMULATIVE COMPETITION
DOLLARS FY85



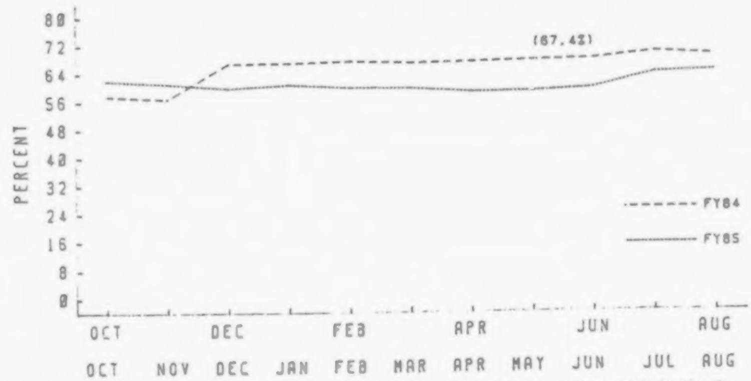
	OCT	NOV	DEC	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG
TOTAL $	557	1655	2359	3132	3583	4435	5232	6123	6815	7937	9493
COMP $	200	538	761	997	1179	1474	1683	1924	2136	2605	3044
COMP %	35.9	32.5	32.2	31.8	32.9	33.2	32.2	31.4	31.3	32.8	32.1

(DOLLARS IN MILLIONS)

Figure 3

While we measure our success in terms of dollars awarded competitively, we also look at contract actions (Figure 4). The total number of competitive actions for Fiscal Year 85 has been lower than our experience in Fiscal Year 84. However, what was a downward trend reversed in May and a significant improvement was made by the end of August. The current trend should produce results like Fiscal Year 84 when 67.4% of our contract actions were competitive.

CUMULATIVE COMPETITIVE
ACTIONS FY85

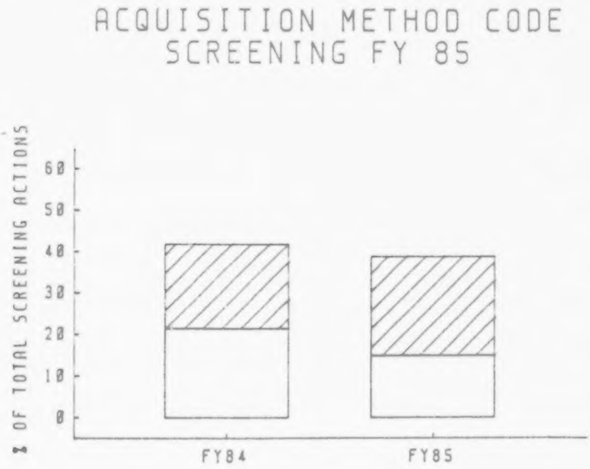


	OCT	NOV	DEC	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG
ACTIONS	14.0	32.0	44.7	69.0	90.1	112.7	135.4	168.4	189.7	235.2	264.0
COMP %	61.9	60.9	59.6	60.6	59.6	59.5	58.3	58.4	59.3	63.6	64.0

(ACTIONS IN THOUSANDS)

Figure 4

The Competition Advocate organization reviews items to assure they are competed if practical, or acquired from the actual manufacturer where appropriate. During Fiscal Year 84, over 60,000 items were screened for code assignment (Figure 5). Over 40% (25,523) were coded for competitive acquisition. Even more significant, is that 47% of those (12,564) were coded competitive for the first time. During Fiscal Year 85 nearly 62,000 items were screened and 61% of those items coded for a competitive buy were coded competitive for the first time. We're making excellent progress.



TOTAL ACTIONS	60,677	61,984
COMPETITION ☐	25,523	24,333
FIRST TIME COMPETITION ▨	12,564	14,812

Figure 5

Proprietary Data

An effort related to the screening of items, which also increases competition, is challenging proprietary claims on existing technical data packages and improving deficient data packages to make them suitable for open competition. The Competition Advocate also performs this function. Successful requests for contractor release of proprietary data rights have increased during Fiscal Year 85. For example, in Fiscal Year 85, Warner Robins Air Logistics Center had obtained release in 100 cases compared to 33 for all of Fiscal Year 84. Of the 133 releases for both years, 79 were granted with no charge. In one of those cases, limited rights previously claimed for a single drawing impeded competition of engine mounts for the C-130 aircraft. The contractor released the rights without charge, enabling future competitive acquisition and potential savings of $13 million.

Reverse Engineering

Where we are not successful in challenging limited data rights and cannot buy them, we prepare those drawings and specifications by physically examining, measuring, and analyzing an item. Our main effort will be through a special program we call Contracting Out Reverse Engineering (CORE). We expect to improve the competitive position of hundreds of items with a savings of many millions of dollars. An additional benefit of reverse engineering is that it is convincing contractors that the

Air Force is serious about competition. Some previously adamant contractors are releasing their rights and others are reducing prices.

Organically, we are using reverse engineering to improve deficient data packages to make them "competable." Warner Robins has successfully completed 126 projects with an annual buy value of nearly $8.7 million. The corrected data deficiencies ranged from missing dimensions to inadequate test data, and we expect some $2.2 million in savings the first year.

Zero Overpricing

Another effort which has been instrumental in reducing procurement costs is our Competition Advocate's support of the Air Force Zero Overpricing Program. Under this program, all Air Force people are encouraged to challenge the price charged when they believe it is overpriced. These challenges are reviewed at base level and, if they appear to be valid, are referred to the central source of supply. This program also provides monetary awards and other recognition to individuals who submit successful challenges. The program began in 1979 and has seen substantial growth, from some 2,700 Air Force-initiated challenges in the first year to over 11,600 in Fiscal Year 1984. Nearly 7,300 challenges were submitted through June of 1985.

Investigating and responding to challenges is a difficult and time consuming process but the results are encouraging. In one case, after a challenge by a sergeant, a subsequent price appraisal by one of our Competition Advocates confirmed that too much had been paid for an extender board. Contracting officials then asked the contractor who supplied the board for a voluntary refund. The company responded and returned $62,381. In the first nine months of Fiscal Year 85, the Air Force has realized over $7.4 million in savings and made nearly 500 monetary awards to those who submitted successful challenges.

I must point out that what we're doing in terms of source development, engineering data management and acquisition method code screening have, for the most part, been done in the past. The manpower increases we've made for the Competition Advocate (from 160 in FY83 to the 1,480 in FY86) have been the key to increased quality and quantity of screening, thus increasing competition and breakout. We must, however, keep in mind that we will always have some situations where competition or breakout is not possible such as where an item's design is unstable or safety of flight considerations are involved.

The Competition Advocate Program has increased the awareness of our work force of the value of an item by emphasizing the opportunities and benefits of competing an item, developing new sources, or buying direct from the actual manufacturer.

Buying Practices

Besides the need to increase competition, the second major objective of the AFMAG recommendations was to insure that the Air Force pays a fair and reasonable price for each spare part it buys. Small quantity purchases and certain pricing techniques were the major factors driving some spare parts prices far beyond their intrinsic value. Past underfunding of requirements and our failure to consolidate quantities for economic buys had been previously identified as contributors and were also highlighted by AFMAG.

We approached this objective by addressing both our buy practices and our pricing procedures. In other words, we're also concentrating on assuring that the prices we do pay are fair and reasonable.

In FY84, for the first time in AFLC, we issued special buy guidelines to our Air Logistics Centers to emphasize multiyear contracting, yearly buys, and consolidation of requirements. All of these improved buy practices are possible only because of improved spares funding. In the earlier environment of extreme underfunding, procurement of economic order quantities was impossible.

One of our more significant initiatives results in much smarter buying of parts. In the past, we were driven, primarily by a lack of complete funding, to buy smaller quantities more frequently. This practice continued even when the funding of spare parts improved in late 1982. With the improved funding level for spares, we have now mandated that, on those smaller dollar value items of stable usage and design, we will buy at least a full year's requirement. Many of the suspected overpricing cases of the past could be directly attributed to the buying of very small quantities of an item rather than an economic production quantity. The key resolution of this problem is adequate funding. Collectively, we are solving this problem and will continue to revise policies and data systems to insure it remains solved.

Another of our initiatives calls for the consolidation of items to be purchased from the same firm or to be purchased competitively from the same firms. This initiative not only provides a better opportunity to reduce cost and make a better buy, but it also makes the buying process administratively more efficient for both contractors and the Air Force.

A major focus of the buy guidelines is expanding multiyear contracting to the buying of spare parts. Although this initiative was started before the recent concern about spares pricing, its use for buying spare parts was given greater momentum. In FY84, we achieved 29 multiyear awards with a total estimated savings of $1.8 million dollars. We are not satisfied with the results of our initial efforts in this area or with the number of multiyear contracts we awarded during 1984. But, it was a start in the right direction. Although FY85 data is not yet available, we believe we have made additional progress, and we have ongoing initiatives to further improve our methods for identifying candidate items for multiyear buying.

Pricing

Pricing practices of the past were developed to cope with workload that increased without commensurate increases in manpower. Many of the overpricing allegations were the direct result of these past pricing policies. For example, a buy of 100 line items would be priced by concentrating our effort on the few high dollar value line items representing 80 to 90 percent of the dollar value of the total requirement. These few items would be priced very carefully. The buyer would then compute the percentage difference between the price proposed and the price negotiated for these few items and apply that price difference to all the other proposed prices in the purchase. While the total contract price was properly determined fair and reasonable, the individual unit prices of many of the items in the total contract were not always representative of the true value of those items. Some line items were individually overpriced. We have now implemented new pricing policies and procedures that will insure unit price integrity of each of the items in the buy. Here are some of our initiatives in the pricing arena.

For negotiated purchases under the threshold for contractor submission of certified cost and pricing data our Spares Management Analysis and Review Technique (SMART) applies. This pricing technique provides the buyer an economical approach to pricing small purchases and negotiated purchases, and insures each part is fairly priced.

For larger purchases, involving many separate items, our Price Analysis and Review Technique for Spares (PARTS pricing) applies. This concept, initially developed by AFMAG, has been implemented in AFLC. It assures that every line item on an applicable sole source contract is reviewed and analyzed. It applies to the pricing and negotiation of orders for spare parts which, after Competition Advocate screening, remain sole source. First, high dollar value items are individually priced, using cost and price analysis supported by Department of Defense contract auditors' review. Remaining items of low dollar value receive a subjective assessment of value and are compared to an illustrated parts breakdown, picture, drawing or sketch of the item, including a short written description of labor, material and engineering characteristics. This review will determine if the price offered by the contractor appears fair and reasonable. Those items failing this test are then subjected to the same cost and price analysis as the high dollar parts. Those passing the test are sampled and analyzed to determine what percentage reduction should be applied to these parts to reflect any overall negotiated price reduction and to assure price reasonableness. All items are value reviewed.

Price Refunds

These are just some of our pricing initiatives to address the major problem areas, but they are not all inclusive. Of course, we have been and will continue to seek voluntary, and involuntary, refunds where we discover overpricing to have existed. In those cases where overpricing occurs, we ask the contractor to refund the excess voluntarily. For example, in FY84, we received less than $75,000 in voluntary refunds, but through August of FY85 we've recovered nearly $6.5 million. Where the overpricing stems from the contractor having misrepresented costs, we pursue price adjustments for defective pricing. In FY84, we recovered over $7 million, and through

March 1985, we've recovered over $1 million. We currently have nearly 100 active defective pricing cases.

PACER PRODUCE

We've also taken steps to place additional manpower in the contracting function. In FY84, we stated a program called "PACER PRODUCE." A first increment of some 300 people were recruited, hired and trained in the basics of DoD contracting to offset our severe manpower shortages. Our aim was to get the best people available to supplement the spares acquisition work force.

In FY85, we hired a second increment under PACER PRODUCE II, in which almost 450 more were placed in the contracting and pricing functions at our Air Logistics Centers. In our current effort (PACER PRODUCE III), about 180 additional new hires are being recruited.

These people joined an existing contracting work force of professionals, almost 65 percent of which have at least a bachelor's degree. Over 95 percent of these PACER PRODUCE trainees have college degrees.

PACER PRODUCE has freed more experienced buyers to handle the most complex buys and concentrate on pricing and negotiating, assuring that fair and reasonable prices are paid for spare parts.

Data Systems

We have been accomplishing our procurement processes with data systems that were put in place over fifteen years ago. While we have updated these systems from time to time, a fifteen-year-old system is inefficient compared to those of today's technology. The demands of our fast-paced, rapidly growing contracting workload far outstripped the capabilities of these data systems. The old systems cannot handle a wartime surge in contracting workload, they do not give our buyers and managers the information or tools they need to effectively price and manage spare parts and they cannot be easily modified or expanded to handle changing information requirements.

Each of our Air Logistics Centers now has a standardized Automated Contract Preparation System (ACPS). The system uses laser equipment for high-speed printing and a menu-assisted data entry system (MADES) to help clerks quickly prepare complex contractual documents. The system has worked so well that several other government agencies have looked at adopting it for their own contracting activities.

We are also in the process of installing the first phase of the Contract Data Management System (CDMS) that will give our contracting people several badly needed capabilities like on-line access to the contracting data in our current systems as well as tools to assist them with spare parts pricing and negotiations. The system is currently being installed and tested at all Air Logistics Centers and AFLC. Over the next five years the contracting data management system will replace outmoded contracting systems with an efficient, totally integrated contracting data base.

To date, our automation initiatives in contracting have reduced manual efforts, given us more accurate data, and helped us cope with a growing workload. The initiatives we are working now will help us negotiate better prices, reduce administrative lead times, and provide wartime surge capability.

Results

As a bottom line to all this, I'm happy to be able to tell you we are now doing an even better job than we've done before. We're doing a better job identifying what we need to buy, a better job buying, and we are saving a lot of money as a result.

Savings

In FY84, after comparing the prices we actually paid with prices we paid in FY83, we calculated an estimated savings of $529 million--auditable actual savings that enabled us to buy more of our needs than would have otherwise been possible and to eliminate what otherwise would have been shortfalls in defense readiness. Through the first three quarters of FY85, we achieved additional estimated savings, again calculated against the FY83 baseline and adjusted for inflation, of over $500 million. That totals to more than $1 billion in verifiable savings from all these initiatives.

The initiatives to use multiyear contracting, buy at economic quantities, and buy one-time-a-year on total needs can now be undertaken because budget programs are, for the most part, being adequately funded. Although some increases in personnel resources have been provided to address specific high visibility problems, the lack of adequate, trained manpower to cope with an increasingly complex and demanding environment is an increasing problem. If funding levels are allowed to slip back to the lean years, less efficient, more costly ways of doing business will also return. Adequate, stable funding and adequately manned contracting offices are critical to continuing our cost saving initiatives.

However, all these initiatives and the extensive reforms in general have had significant impact on the Logistics Command.

Lead Time--Effects

Average administrative lead time is the average number of calendar days it takes the Air Logistics Centers from the receipt of a purchase request document in the buying office to the award of a contract. As you can see in Figure 6, average administrative lead time for all buys in AFLC increased from 54 days in May 1983 to a high of 133 days in April 1985, and has now decreased to 116 days--still substantially higher than FY83. As we assimilate many of the shocks to our system that were caused by all of the changes we have discussed, we expect the average to drop further, but still be at least 50 percent higher than FY83. It is also clear from the "under $10,000" buy trend line that this increase has occurred in both small and large dollar value contracts alike. Since mid-1983 increases in administrative lead time have been dramatic. These increases reflect the cost of contracting because each additional day of pipeline (the flow of goods and services needed to maintain the Air Force at an acceptable level of readiness) requires an estimated expenditure of about $7.5 million in stock funds, and approximately $3.8 million of investment funds. Lead times must be brought back in line as quickly as possible.

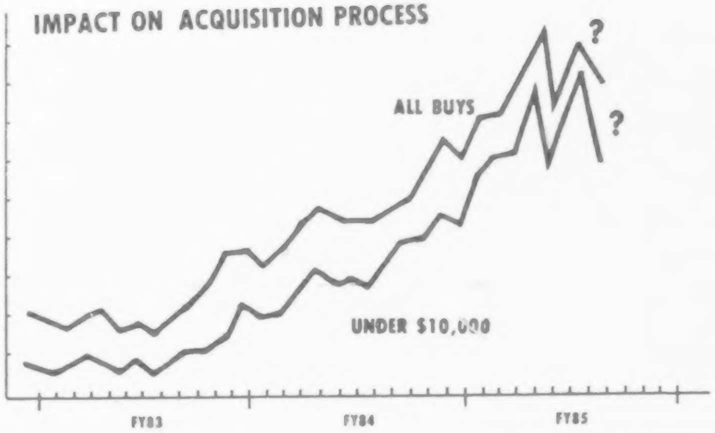


Figure 6

Increasing administrative lead time is a serious concern because of its impact on field support, program execution, unpriced actions, and the budget. As the number of days lead time expands beyond the number of days included in our requirements computations, we will have a gap in the pipeline downstream and will require unusual management actions to avoid a breakdown in supply support. Also, as we take longer to award contracts and as requirements continue to generate, we experience an increase in on-hand workload in our buying offices which in FY85 had an unprecedented high level of work in process.

Our capability of obligating funds at an acceptable rate is reduced as lead times increase. The larger dollar value contracts that obligate most of our funds generally take longer and the average lead time for these approached 300 days in FY85.

To offset unanticipated lead time increases as well as unanticipated needs, and to avoid supply support gaps downstream as mentioned earlier, using unpriced actions becomes essential.

Finally, the budget is significantly affected by lead time. Unpredicted lead time increases can result in shortfalls as our actual requirements computation generates larger quantities to fill the extended pipeline. We have periodically adjusted our computation factor to compensate for increasing lead times and have recently placed a floor of nine months lead time in all computations to avoid downstream support problems.

Lead Time--Causes

We find five primary causes for the increase in administrative lead time: Change Adaptation, Lack of Qualified Manpower, Validating Previous Prices Paid, Pricing Each Item, and Psychological.

We can blame some of this increased lead time on delays inherent in adapting to the changes being made throughout the contracting community. The growing shortfall in manpower mentioned earlier followed by the hiring and training of a significant number of additional new people severely trailed our needs and affected our overall ability to perform. The requirement to validate past prices paid to make sure all prices appear reasonable when compared to the actual item, and the necessity to establish unit prices representative of the value of each item being bought, even on our small purchases, have extended the time spent in negotiating all contracts. These reviews will have a long-term payoff by reducing negotiation time the next time we buy an item that has already been reviewed in this way. Finally, and perhaps the largest contributor to the increasing lead time, is the psychological factor, the extra caution being taken by government workers and defense contractors alike. No one wants to be involved with the next "spare parts overpriced horror story."

Our goal is to continue the reform process, insuring that the changes that are helping to improve the process and reduce the cost of defense are fully institutionalized. But we can no longer ignore what has been happening to administrative lead time. We must find ways to continue the improvements and reduce administrative lead time. Within the spirit and context of this goal we offer the following recommendations.

Recommendations:

Before we go into the specific recommendations, one point needs to be stressed. We have limited ourselves to only those recommendations we believe could have a favorable effect on administrative lead time.

Near Term

On the legislative side, AFLC recommends removal of the impediments shown in Figure 7.

Low Dollar Impediments

It simply doesn't make sense to publicize extensively small purchases that are already competitive or are of such low dollar value that they cost an excessive amount to buy compared to the value of the items being bought. And giving everyone a bid package that wants one is not cost effective. In fact, the basic concept of full and open competition that came with the Competition in Contracting Act needs to be reevaluated. Once you achieve adequate and effective competition, increasing the number of bidders will normally not be cost effective, especially on the smaller dollar value contracts. The thresholds for publicizing requirements should be raised to $25,000 consistent with the legislative intent to simplify small purchases. Public Law 95-507 should be changed to permit limiting bidders on small dollar value actions. Additionally, Public Law 98-577 should be amended to eliminate the requirement to refer small business nonresponsibility determinations to the Small Business

Administration for a Certificate of Competency for actions below $25,000. Similarly, many of our social-economic thresholds such as contained in the Walsh-Healey or Davis-Bacon Acts could be raised to apply only to acquisitions over $25,000.

NEAR TERM RECOMMENDATIONS

- REMOVE LEGISLATIVE IMPEDIMENTS THAT PROVIDE MINIMUM BENEFITS
  - •• RAISE PUBLICIZING THRESHOLDS
  - •• RESCIND BID PACKAGE REQUIREMENTS
  - •• RESCIND SMALL PURCHASE COC REFERRAL TO SBA
  - •• RESCIND REQUIREMENT FOR SUB-CONTRACTING PLANS
  - •• ABOLISH PROCUREMENT CENTER REPRESENTATIVES
  - •• DELEGATE J&A > $10 MILLION TO HCA
- LEGISLATION SHOULD BE POLICY RATHER THAN REGULATORY

Figure 7

Subcontracting Plans

The requirement for subcontract plans in contracts of $500,000 or more imposes more work and higher administrative lead time and cost without evidence of increasing small business' piece of the pie. Subcontracting plans and goals should be on a plant-wide basis. The requirement for procurement center representatives totally duplicates our competition advocates without hope of any additional payoff to offset loss of lead time. Decentralization of authority is important to efficient acquisition processes and approval of Justification and Approvals for other than full and open competition under Public Law 98-369 at levels of management higher than the MAJCOM will not have an appreciable effect on acquisition plans but could delay the acquisition process 60 - 90 days. Contracts over $10 million are small in number but involve nearly 60 percent of the AFLC dollars obligated annually, which affects program execution as well.

Debt Collection Act

The Debt Collection Act of 1982, Public Law 97-365 (31 USC and 3701 et. seq), has been held by the Armed Services Board of Contract Appeals to apply to Government contracts, even though little evidence supports such a determination. This determination renders ineffective the Government's common law right to offset the amount owed to the contractor from the amount due to the Government because of unacceptable performance or other reasons. The Act should be amended to exclude its application to Government contracts, since Congress had previously provided applicable procedures in the Contract Disputes Act.

CICA

An eighth exception to Full and Open Competition needs to be added to CICA for engineering critical items that have potential significant impact on safety or mission accomplishment for which we do not have the technical capability or data to describe the item or its qualification standards. We need the exception so we can procure such items competitively with reasonable assurance that their use will not result in loss of life or limb or bodily injury, or cause significant property damage; and such items should also be exempt from the qualification requirements of Public Law 98-525 (10 USC 2319) (see FAC 84-11).

Freedom of Information Act

The Freedom of Information Act needs to be amended to add another exemption to allow withholding of procurement-related, commercially-exploitable material.

Long Term Objective

Finally, in general, legislation should establish broad policy guidelines and permit the agencies some flexibility to establish the specific regulatory language to implement that policy. Although we are convinced the approval of the near-term recommendations will have an immediate positive effect on administrative lead time without negatively affecting the good results of our overall efforts to improve the acquisition process, we believe a longer term objective is absolutely essential in making permanent improvements.

Decentralization, Commercialization, and Simplification

All those involved in regulating the Federal acquisition process need to return to the basic principles of decentralization, commercialization, and simplification.

Centralization is not the solution to big business problems, nor is it the way to get one's arms around the Federal acquisition process. A number of studies, such as the Commission on Government Procurement of the early seventies, emphasize the importance of centralized policy making with decentralized execution of that policy. This principle, especially decentralization of execution, needs to be considered favorably in future reform efforts. Follow-up audits and reviews can ensure compliance with the law and to hold managers and contracting officers responsible and accountable for their actions.

Standard commercial practices should be preferred over the inventing of new bureaucratic complexities whenever practical.

Reform should make the system easier to access and simpler to manage. While that has occurred with some of the recent reforms, the overall magnitude of the reform effort has created additional major complexities.

Finally, reform efforts should be careful not to destroy the relationship that exists between the Defense Department and the Defense industry. A healthy "arm's length" relationship is absolutely vital to maintaining the defense posture and mobilization capacity of the United States.

Competition Limits

In addition to embracing these three themes, future reform efforts also need to avoid two areas. Future reform efforts must both recognize the limits of competition and provide policy direction without legislating mandatory specific requirements. We can categorize the limits to competition into three distinct areas.

First, we encounter technical limits where the skill and expertise needed by a second source to manufacture the item are not available. Examples here would include certain engine blades, landing gear, and various bearings.

Then, we run into business limits, where the knowledge of, for instance, certain manufacturing processes, does not exist outside the existing brain trust. These would include the small and mid-range business size companies for which this intellectual brain trust serves as the "company jewels." An example here would be the Delevan fuel nozzle.

Finally, we find economic limits, where the time and money needed to establish additional sources are not available or justifiable.

The bottom line is that the competition decision must be made on a part-by-part basis, and competition in and of itself should not be the goal or objective of any procurement reform effort.

Finally, future reform efforts must provide general policy direction and not specific regulatory directives. Any law that arbitrates specific action, whether a percentage goal to be achieved, a mandatory review to be accomplished at a very high level, or any other specific level of accomplishment that provides no flexibility for applying good common sense when the directive being implemented is not a good statute. That reform will not benefit the acquisition process, and the ultimate cost will be paid by the body we--both Congress and the Defense Department--are trying to benefit the taxpayer.

Any major reformation of the Federal acquisition process should adopt these long-term objectives.

Conclusion

Finally, I want to emphasize that the Air Force Logistics Command is fully committed to resolving the pricing concerns raised by Congress, the Administration, and the American taxpayers. I think we have proven this commitment by increasing required manpower resources to accomplish increased breakout and competition and to improve pricing of spare parts, by spending increased dollars up front to achieve greater savings in the long term, by implementing extensive changes wherever needed throughout our acquisition procedures, and by acquiring new and up-to-date automatic data processing equipment.

We have undertaken all these positive steps within existing legislative guidelines, to assure the items we buy are reasonably priced while at the same time being careful that the necessary changes are made without disrupting the Air Force's primary mission.

Our efforts to date are achieving very significant benefits. The steps we have taken and continue to take are directed toward providing needed logistics support at the lowest cost.

We are firmly committed to continue our efforts to develop more and better ways to acquire, efficiently and economically, the Air Force's requirements; but, we must not lose sight of the ultimate purpose of our efforts--that of supporting the Air Force's readiness and sustainability initiatives. We will most certainly continue our search for new and better ways of getting our job done; but, we must always be careful not to achieve acquisition efficiencies to the detriment of the very purpose for which we acquire spare parts--to insure that we stand ready as a nation to execute our war plans effectively when needed.

We now need time to train our people fully and to implement these reforms and complete the institutionalization process intelligently.

Mr. Chairman, this concludes my prepared statement.

Senator QUAYLE. Thank you, General.

The next witness is Admiral Hughes, Deputy Chief of Naval Operations, Logistics.

STATEMENT OF VICE ADM. T.J. HUGHES, U.S. NAVY, DEPUTY CHIEF OF NAVAL OPERATIONS, LOGISTICS

Admiral HUGHES. Good morning, Mr. Chairman and members of the Senate Armed Services Subcommittee on Defense Acquisition Policy.

I am Vice Adm. Tom Hughes, Deputy Chief of Naval Operations, Logistics, and the Navy's joint logistic commanders' representative.

It is an honor and a pleasure to appear at this Senate hearing to discuss with you our views on the impact of recent legislation on how we do business.

I have submitted a statement for the record and request that it be so entered. Subject to your approval, Mr. Chairman, I will provide a brief oral overview of that statement.

Senator QUAYLE. It will be placed in the record.

Admiral HUGHES. The Navy supports the legislative intent of the three public laws which are the subject of the subcommittee's review. Further, the Navy generally supports the initial conclusions of the joint logistic commanders as represented in the "pendulum" briefing alluded to by General O'Loughlin in his complete statement for the record.

With respect to the Competition in Contracting Act of 1984 [CICA]—Public Law 98-369—the Navy has adjusted its way of doing business by eliminating determination and findings for oversight of our procurement actions and reoriented our oversight of the acquisition process by the active participation of the Assistant Secretary of the Navy, Shipbuilding and Logistics, in the selection of the acquisition plan as the principal document for program review and oversight.

Approval of the acquisition plan is granted through the issuance of a program endorsement memorandum signed by the appropriate acquisition executive, an Assistant Secretary of the Navy. Prior to approval, these acquisition plans are reviewed by the Navy's competition advocate general. This facilitates the review and approval process of the justification and approval statements required by CICA.

With regard to the Defense Procurement Reform Act of 1984—Public Law 98-525—we have a minor concern for the scope of the law's applicability, particularly where publication of some pricing guidance could be detrimental to the Governor's interest in competitive bidding. Clarification of this aspect would be helpful.

Another aspect of concern is the potential complexity involved in establishing and effectively administering warranty provisions in our contracts. We follow the DOD for supplement criteria requirements and include warranty in our contracts to the maximum degree possible. Only time and experience will reveal our ability to manage this process effectively.

The Small Business and Federal Procurement Competition Enhancement Act of 1984—Public Law 98-577—raised two issues. The first concerns the use of breakout procurement center representatives. Currently one breakout procurement center representative and at least two technical advisors are targeted for placement at eight Navy procurement centers.

The duties of these personnel appear to be duplicative of the activities competition advocates and breakout personnel, and to a lesser degree, to those of small and disadvantaged business utilization personnel. We will have to see how this arrangement works in practice and adjust duties accordingly.

The second issue is the requirement for referral to SBA for certificates of competency [COC] which is perhaps not even executable. Referral of small dollar value requirements is impractical. We would like to see a threshold of $25,000 established for this requirement.

Further, we support an amendment to the COC process which would eliminate referral at all dollar values if, after a nonresponsibility determination, the bidder-offerer next in line for award is also a small business concern.

The Navy has viewed irregularities in the acquisition process seriously and has made a major organizational adjustment to streamline the decisionmaking process. A major impact of this reorganization is an improved opportunity to affix accountability in program management.

We have taken the lead in focusing on competitive practices within the Department of Defense. In July of 1983 the Secretary of the Navy established a Navy competition advocate general who reports to the Assistant Secretary of the Navy, Shipbuilding and Logistics, and competition advocates have been appointed to all buying activities with procurement authority over $25,000.

Navy competition initiatives in shipbuilding have resulted in over $2.5 billion of savings since fiscal year 1983. Navy competition—on dollar value basis—has increased from 26.7 percent of the dollar value in fiscal year 1982 to approximately 44 percent in fiscal year 1985.

We estimate that more than one-half of the dollar and two-thirds of the actions in fiscal year 1986 will be competitive. We are now putting in specific disciplines to make sure that low technology items are not experiencing excessive cost due to overspecifying.

In August 1983 the Navy initiated "Project Buy Our Spares Smart" to attack the problems which caused excessive prices for spare parts. Navy initiatives to break out spare parts, compete requirements to the maximum extent practicable, and improve all phases of the materiel acquisition process resulted in documented cost avoidance of $378 million through August 1985 at a cost of $101 million investment.

Finally, to put our efforts into perspective, you should be aware that in fiscal year 1984 our professional GS-1102 work force of 3,636 people processed 73,472 actions in excess of $25,000, and played a major part in the obligation of $45.4 billion, 1984 expenditures. Fiscal year 1985 statistics are quite similar.

Our acquisition people are doing an incredible job, and have adjusted, and will continue to adjust, to a changing environment. We continue to support legislation reforms, but suggest that we be given time to allow us to establish implementing guidance for these three principal legislative initiatives before attempting to go further with the reforms. It takes time to codify and implement major changes in guidance.

I will be pleased to answer any questions you may have. Thank you.

[The prepared statement of Admiral Hughes follows:]

Prepared Statement of Vice Adm. Thomas J. Hughes, U.S. Navy, Deputy Chief of Naval Operations (Logistics)

Good morning. I am Vice Admiral Tom Hughes, Deputy Chief of Naval Operations, Logistics and the Navy's Joint Logistics Commanders representative. It is a pleasure to appear at this Senate hearing and discuss with you our views on the impact of recent legislation on how we do business. I intend to give a Navy slant on our concerns with Public Laws 98-369, 98-525, and 98-577. I also wish to emphasize that the Navy generally supports the Pendulum initiatives.

The Navy supports the legislative intent of the Competition in Contracting Act of 1984 (CICA) (Public Law 98-369) of increasing competition in the acquisition process. Prior to CICA, we relied in large part on the approval process for determinations and findings (D&Fs) for oversight of our procurement actions. With the elimination of D&Fs for negotiation authority under CICA, the Navy reoriented its oversight of the acquisition process. The Assistant Secretary of the Navy (Shipbuilding and Logistics) (ASN (S&L)) selected the acquisition plan (AP) as the principal document for program review and oversight. Navy contracting officers support the program manager in preparation and maintenance of the AP. The contracting officer ensures that the acquisition strategy is both realistic and achievable. We require review and signature by the Head of the Contracting Activity (HCA), program manager, Chief of the Contracting Office and contracting officer. Approval is granted through issuance of a Program Endorsement Memorandum (PEM) signed by the appropriate acquisition executive, an Assistant Secretary of the Navy. Prior to approval, these APs are reviewed by the Navy's Competition Advocate General.

The thorough scrubbing of the AP by the Secretariat staff, Competition Advocate General, and others facilitates the review and approval process of the Justification and Approval (J&A) required by CICA. The Navy's Senior Procurement Executive, ASN (S&L), approves J&As in excess of $10 million. Our view is that comprehensive reviews of APs and J&As through the Navy's approval process will result in effective advance planning of proposed contract actions resulting in good acquisition strategies, compliance with sound practices and policies, and increased competition.

Let me briefly discuss the Defense Procurement Reform Act of 1984 (Public Law 98-525). One area of concern centers on the requirement for publication of proposed regulations. While we certainly agree with a need for a comment period for those significantly impacted by policy, regulation, procedure or form, we feel there is a need for clarification as to the law's applicability.

Another aspect of this legislation receiving much attention in the Navy is the warranty coverage. The Navy supports a strong and equitable warranty program as a tool to encourage contractors to increase the use of quality design and manufacture. We apply the requirement of weapon systems to those systems listed and defined in the DOD Federal Acquisition Regulation Supplement (includes aircraft, missiles, ships, military cargo vehicles, military surveillance systems, command and control, communications, fire control systems, electronic warfare, and propulsion systems). Other items to be warranted are selected by the contracting activity in accordance with existing DOD FAR Supplement criteria requirements. The Navy believes in a comprehensive warranty program and includes warranties in our contracts to the maximum degree possible. We are concerned with the complexity involved in establishing and effectively administering warranty provisions in our contracts.

The Small Business and Federal Procurement Competition Enhancement Act of 1984 (Public Law 98-577) raised two issues of interest to the Navy.

The first issue concerns the use of Breakout Procurement Center Representatives (BPCRs). Currently, one BPCR and at least two technical advisors are targeted for placement at eight separate Navy procurement centers. We have little experience in this area upon which to assess the impact of these Small Business Administration assignments. Most of these assignments have been made during the last 30 to 60 days or are yet to be made. We can make a case that the duties of the BPCRs and their technical advisors will be duplicative of the actitities' competition advocates and breakout personnel and, to a lesser degree, to those of the small and disadvantaged business utilization specialists. Notwithstanding a potential for becoming duplicative of Navy initiatives and contributing to procurement administration lead time, the program may also offer an opportunity to supplement limited Navy resources with those of the SBA. The impact of this program cannot be ascertained until fully implemented.

The second issue revolves around the requirement for referrals to SBA for Certificates of Competency (COCs). We strongly believe that referrals of small dollar value requirements for COC actions are impractical and not in keeping with sound business practices. Such action defeats the stated purpose of small purchase (actions less than $25,000) procedures of reducing administrative costs and increasing opportunities for small business concerns. SBA previously recognized the impracticality of low dollar referrals by providing for an "under—$10,000" exemption from the COC process. The added administrative burden and the additional time required to process COCs for small dollar actions clearly makes a case for some flexibility in this area. the Navy would like to see a $25,000 threshold established whereby actions less than this dollar amount would not be subject to COC procedures. In addition, we support an amendment to the COC process which would eliminate referrals at all dollar levels if, after a nonresponsibility determination, the bidder/offeror next in line for award is also a small business concern.

I now would like to briefly comment on some of the Navy's efforts to accomplish reforms.

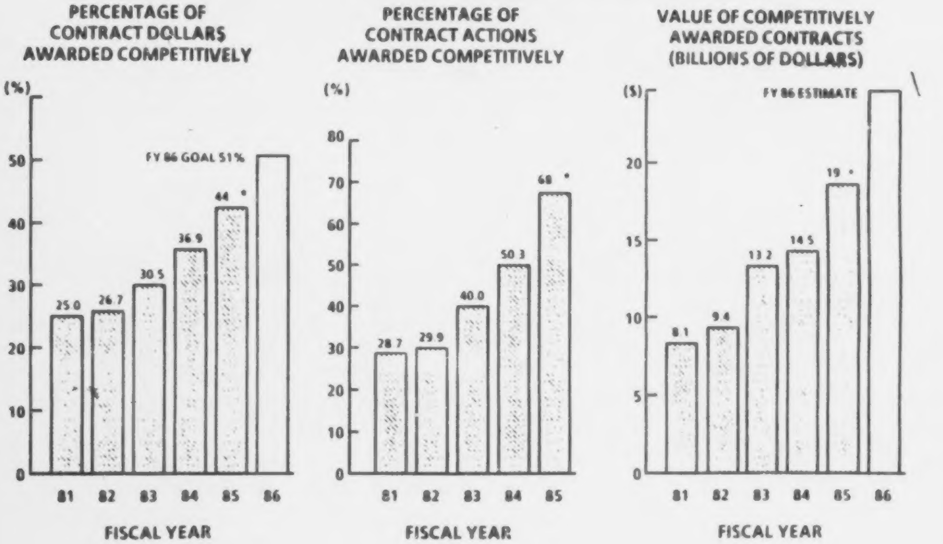
In order to minimize problems associated with organizational layering, the Navy made a major change to its acquisition management structure in April 1985. This change involved the elimination of some of the Navy's organizational strata in order to streamline the decision making process. A major impact of the reorganization is an improved opportunity to affix accountability in program management. The material systems commanders have direct access to the Secretary of the Navy and Chief of Naval Operations who will exercise direct oversight and policy control.

Another area in which we have made great strides is competition. We have taken the lead in focusing on competitive practices within the Department of Defense. For example, in July 1983, the Secretary of the Navy announced the establishment of a Navy Competition Advocate General, a Flag officer who reports to the Navy Senior Procurement Executive, the Assistant Secretary of the Navy (Shipbuilding & Logistics). Competition advocates also have been appointed at all buying activities with procurement authority over $25,000. In addition. more than 150 competition advocates have been designated at field activities which generate more than $1 million in annual procurement requirements.

Results of Navy competition initiatives continue to be impressive, with cost savings in shipbuilding since fiscal year 1983 of over $2.5 billion. Examples of savings in major programs include $248 million from fiscal year 1983-1985 competitions for nuclear attack submarines; $840 million for AEGIS cruisers; and $55 million from the fiscal year 1985 competition for the Vertical Launch System.

Navy competition has increased from 26.7% in fiscal year 1982 to approximately 44% through fiscal year 1985. We estimate that more than half of the dollars and two thirds of the actions in fiscal year 1986 will be competitive. I am including as part of my statement three graphs showing the year-by-year improvement that has occurred. We consider increased competition as a key to continued improvement of our acquisition system while obtaining lower costs, better cost control, higher quality, improved schedules, and a stronger industrial base.

DEPARTMENT OF THE NAVY
PROCUREMENT COMPETITION PERFORMANCE



* PRE-CLOSEOUT ESTIMATE

DATE: OCTOBER 1985

PREPARED BY THE
OFFICE OF THE COMPETITION ADVOCATE GENERAL

In August 1983, the Navy initiated Project Buy Our Spares Smart (BOSS) to attack the problems which cause excessive prices for spare parts. Over 100 individual actions were undertaken to highlight and resolve conditions which promoted higher prices. All Navy personnel were called upon to do their part to use the Federal Supply System, promote competition in the procurement of goods and services and report unreasonable prices.

The overriding objective of Project BOSS is to pay only fair and reasonable prices for spare parts and other material used to support Navy systems. Navy initiatives to break out spare parts, compete requirements to the maximum practicable extent, and improve all phases of the material acquisition process resulted in documented cost avoidances of $378 million through August 1985.

Finally, to put our efforts into perspective, you should be aware that in fiscal year 1984 our professional workforce (GS-1102s) of 3,636 people processed 73,472 actions in excess of $25,000 and played a major part in the obligation of $45.4 billion. The numbers are not dramatically different for fiscal year 1985. Our acquisition people are doing a credible job and have and will continue to adjust to a changing environment. We continue to support legislated reforms but suggest an approach allowing us to establish implementing guidance.

I will be pleased to answer any questions you may have.

Thank you.

Senator QUAYLE. Thank you very much, Admiral Hughes.

The final witness will be the Director of the Defense Logistics Agency, Gen. Donald Babers.

STATEMENT OF LT. GEN. DONALD M. BABERS, U.S. ARMY, DIRECTOR, DEFENSE LOGISTICS AGENCY

General **Babers**. Mr. Chairman and the members of the subcommittee, it is my privilege to be before you today.

I certainly appreciate the interest you have taken in this important subject.

I have prepared a formal statement which has been submitted. I would ask that it be included in the record. I will give you a very brief summary.

Senator **Quayle**. Without objection.

General **Babers**. The Defense Logistics Agency manages over half of the items used by the Defense Department. It buys all of the fuel, most of the food, most of the clothing and textiles, handles about three-quarters of all acquisitions placed on the wholesale system.

We make about 1.4 million procurements a year. That turns out to be 6,000 a day. What is the work force like that handles this today? They are dedicated and conscientious and they want to do a good job just like you and me and everybody in this room.

Fifty-four percent of our nonsupervisory work force among these procurement personnel have less than 3 years with the Government. The significance of that is it takes a minimum of 3 years to recruit, to train these people, to give them the work experiences so that they can work reasonably well on their own.

We have a 16-percent a year attrition rate. We are losing about 16 percent across all acquisition fields to include quality. We have a big training workload. When we looked at that in July last year, we found out we had been foregoing the professional development so necessary for a professional work force, making sure that people stayed with their nose to the grindstone and made those awards and make sure they made no mistakes.

We have almost doubled the training to overcome that backlog. We will do the same in 1986 with the goal of eliminating that total backlog by the end of 1986.

The environment? You have heard it today. We have had to fire. We have had hundreds of changes. Supervisors overseeing that 54 percent of the work force that is below the journeyman level not only have to ensure that those people receive the assistance, the help, the formal training, and the on-the-job training that is so essential, but they also must absorb all of the implications of these hundreds of new acts.

It is a very turbulent situation in which they find themselves. If you look at what has happened in the last couple of years as a result of all these laws, focus on competition, I think you would have to say there have been more beneficial effects than those that would be adverse.

Our savings in 1984 approached $120 million. It looks like we will be about $153 million this year. We don't have the final count on that yet. All that is not free: it costs us something.

I zero baseline at readiness. It takes us longer to make awards now than it did before. We do not want to make as many mistakes. We look for technical data for additional sources. We had a backlog of procurements from 10,000 above the normal accepted backlog in 1983, we are up to 82,000 now.

It has caused a drop in supply availability. We have dropped between 2 and 3 percentage points. It is still high, but it is going to continue to go down. That results in a ship that sails without having the stocks and stores necessary to support it or tanks deadlined for motor parts. We are concerned about that.

I cannot say that what people have imposed on us has caused us to take longer to make those awards. Some of that is our own doing. To ensure that we pay fair and reasonable prices, we have instituted additional supervisory steps and gates through which certain procurement actions must go, again to ensure that we have the best price on any given product.

In addition to that, instead of keeping these inexperienced people at their desks making awards, we send them off to school to make sure they have that professional training. So, we have continued to cause some of our problems in that area.

I think we are a good year or 2 years away from having the competence on that work force that we are after. As I see it, all the rules in the world that we make, all the good intentions, and the extent to which those are successful in cleaning up problems we have in the procurement business depend on how professional our work force is.

I would echo the sentiments of my colleagues here in terms of a more professional work force and recognition of their professionalism.

Concerning legislative requirements, I would like to emphasize only a couple of those, and reemphasize what my colleagues have said.

First, we deal with the certificate of competency and the role that SBA plays; 97 percent of all our awards are valued under $25,000. Most of our actions are in that category.

The new rules of law that are about to be placed into effect will require that the contracting officer cannot make the decision not to award to a low bidder irrespective of poor quality or poor history of delivering quality merchandise on schedule.

Those nonresponsibility decisions will be required to go forward to the Small Business Administration. Today we refer about 400 of those a year to the Small Business Administration. Once this new law goes into effect, we expect there will be somewhere between 33,000 and 40,000.

This is a highly administrative process. It requires time for buyers, the same people who are getting behind schedule, to prepare the documents to go forward to the Small Business Administration It takes 2 to 3 months to process those cases.

The impact will be devastating in terms of administrative workload and in terms of increased backlog. I would ask consideration of the request made by members of this panel.

Again, sir, I would say there has been a lot more good than bad that has come from all these new laws. I would ask for time to assimilate those into our culture. We will keep the emphasis on it.

Thank you for your interest.

[The prepared statement of General Babers follows:]

PREPARED STATEMENT OF LT. GEN. DONALD M. BABERS, USA, DIRECTOR, DEFENSE LOGISTICS AGENCY

Mr. Chairman and Members of the Committee:
I am pleased to have the opportunity to appear before the Defense Acquisition Policy Subcommittee today to discuss the status and impact of the Defense Logistics Agency's implementation of the three principal pieces of legislation passed into law in 1984 which affect Defense acquisition: the Competition in Contracting Act of 1984 (P.L. 98-369); the Defense Procurement Reform Act of 1984 (P.L. 98-525); and the Small Business and Federal Procurement Competition Enhancement Act of 1984 (P.L. 98-577).

BACKGROUND

To place my remarks in context, let me first comment on the nature and scope of DLA operations. Within DLA we manage over 2.5 million consumable items, over one-half of the items managed within DoD, and receive almost 75 percent of the requisitions processed by DoD activities; we support 971 major weapons systems; and we administer contracts for the military departments and civilian agencies. Currently, we have 383,000 such contracts on hand for administration valued in excess of $217 billion. Of these, approximately 1,011 support major weapons programs. Item management is accomplished by our six Defense Supply Centers. Contract administration is accomplished by nine Defense Contract Administration Services Regions. Our contracting workforce consists of almost 4,000 personnel. Our contract administration workforce consists of about 3,300 personnel.

During Fiscal Year 85, DLA awarded in excess of 1.4 million contracts amounting to $15.2 billion. Of these awards, 97.6 percent were valued at $25,000 or less. These actions, however, constituted only 14.2 percent of the total dollars awarded. Our overall competition rate for this period, based on dollars awarded, was 90.4 percent; 3.4 percent above our goal. This represents an increase from FY 83 of 10.3 percent. DLA also aggressively supports the Small and Disadvantaged Business Program. This is reflected in the fact that 74.3 percent of DLA's FY 85 awards were made to small business firms, that received 42.1 percent of the total dollars awarded.

COMPETITION ADVOCATE PROGRAM (THE BENEFITS OF COMPETITION REFORM)

Within DLA, as managers of consumable items, we continue to vigorously pursue efforts to improve competition and achieve cost savings in all our contracting actions. We attempt to do this, not only through implementation of legislative requirements, but through management initiatives as well. Our Competition Advocacy Program consists of the following:

Competition Advocates have been placed in all of our procuring activities and Defense Contract Administration Services Regions. DLA's Competition Advocacy Program, "Improve Pricing and Competition," recognizes that overcoming barriers to full and open competition is the responsibility of everyone involved in the acquisition and logistics process. Our program, therefore, consists of initiatives in the following areas:

o Market research, including Command visits to the Chief Executive Offices of major corporations.

- Competition "hit lists" of historically sole source items.
- Spares break-out to alternate sources.
- Value engineering.
- Publicity to the public, including the conduct of business fairs and conferences.
- Post-award overpricing refund program.
- DoD Parts Control Program.
- Intrinsic value analysis.
- Economic ordering.
- Outreach to small business concerns and participation in trade association functions.
- Employee award program to encourage efforts to enhance competition.

These initiatives resulted in savings totaling $123 million in FY 84. Although all the data is not in yet for FY 85, we project, based on third quarter FY 85 actual savings, that savings from our competition advocacy program will be approximately $153 million for this past fiscal year. These figures do not include $139 million in cost avoidance for FY 84 and $109 million in cost avoidance projected for FY 85.

RECENT PERFORMANCE
(THE COSTS OF COMPETITION AND OTHER REFORMS)

Although our efforts to enhance competition and achieve contract cost savings have achieved considerable success, we have not lost sight of what we are in business for -- to provide responsive readiness support to the military services. The increase in our overall competition rate has not been achieved without cost. Over the course of the last three years, we have experienced an upward trend in procurement administrative leadtime - the time it takes from receipt of a purchase request to award a contract. Further, our contracting workload is growing.

DLA's contracting workload is measured by purchase request line items. Since FY 83, we have added 811 workyears to the contract placement function. However, the number of purchase requests continues to increase despite this added manpower. In FY 83, DLA awarded 3,548,160 line items. In FY 85, we awarded 3,576,577 line items. Our FY 83 end of the year backlog was 10,700 lines. At the end of FY 85, that backlog was 82,700 lines. This trend has been steadily on the rise. Further, during FY 83, our supply availability, or our ability to respond to customer demands, was 91.8 percent. Supply availability dropped to 91.1 percent during FY 84. This past fiscal year our supply availability declined to 89.1 percent. The decline in supply availability over the last year is, we believe, due in large part to the steady upward trend in leadtime which we have experienced.

In DLA, spare parts are managed by our four "Hardware Centers." In FY 83, our average Hardware Center small purchase leadtime, excluding purchases made through our small purchase automated systems, was 71 days. It has steadily increased over the last two fiscal years to a current average of 82 days. In the same four Hardware Centers, large purchase leadtime increased from FY 83's average of 115.3 days to an average of 141.5 days at the end of FY 85.

Increased leadtime increases the commitment authority requirement and may contribute to the need for additional quantities of material to cover safety levels. Since leadtime has been on a steady rise and has not remained stable, we do not have an accurate leadtime figure from which to forecast the quantity we must maintain in stock to cover the leadtime to buy and receive contracted material.

There is no single causative factor to which I can point for these trends. Some of the increased leadtime is directly related to DLA management action to improve the quality of our contracts and to otherwise assure contract price reasonableness. We know, for example, that some of the additional buyer time applied per action to award a contract is being spent providing greater assurance of price reasonableness, on seeking additional sources, and otherwise improving the quality of our contracts. We have renewed our determination to assure that DLA's buyers and contracting officers exercise care in awarding contracts. We are requiring them to spend additional time to assure the highest quality of each contract action. Part of our quality emphasis involves assuring that our contracting personnel have received mandatory training. Training reduces current productive time available, but has subsequent paybacks. We also know that contracting personnel have been subject to significant repeated regulatory changes in the last few years. The transition from the Defense Acquisition Regulation to the Federal Acquisition Regulation in April 1984, was followed only one year later by the major regulatory provisions brought about by CICA. At present, our contracting personnel are facing the implementation of the majority of the provisions of the Defense Procurement Reform Act of 1984 and the Small Business and Federal Procurement Competition Enhancement Act of 1984. Our people must be given the time to absorb and internalize the significant volume of legislative and regulatory reforms implemented in recent years. Only then can they be confident of their knowledge base. Some of the increased leadtime is, however, directly related to statutory requirements.

Whatever the causes for increased leadtime, decreased productivity and decreased supply availability, we have to contain these trends and begin to reverse them.

DEFENSE LOGISTICS AGENCY MANAGEMENT ACTIONS TO REDUCE LEADTIME

In addition to enhancing competition and otherwise achieving contract cost savings, we also attempt to control the costs of doing business and placing contracts through other management initiatives to effect economies and efficiencies in our operations. One of the primary means through which we do this is the use of automated purchasing systems for those small purchases valued at less than $10,000. Maintaining a knowledgeable, educated, professional workforce, is another essential element in our efforts to increase productivity, and thus, our cost effectiveness.

We are taking management action to contain and eventually reverse the adverse trends in leadtime and productivity within my control. I am strongly committed to improving the quality of our contracts, the administration thereof, and the process which generates that result. One of the principal means through which I am attempting to achieve that result is by improving the quality of our contracting and contract administration workforce. In FY 84, we began a concerted effort to develop a truly professional, well trained, better qualified contracting and contract management workforce from which we can increase productivity in the placement and administration of contracts and improve the quality of the contracts placed. We began this initiative in recognition of the fact that almost 50 percent of our contracting and 58 percent of our contract administration workforce hold college degrees or higher. However, 54 percent of our contracting workforce has less than three years of experience, and almost half of our contract administration workforce has less than five years experience in their current professional positions. Our efforts to develop well qualified buyers and contract administrators have included:

- o The creation of "intern" programs as the planned sole source of entry into the contracting and contract management career field. The intern programs consist of selection of highly capable people who are provided formal course instruction together with on-the-job training over a period of one year. Following this training, interns are placed in existing vacant positions. At the conclusion of two more years of contracting or contract management experience, these interns will reach "journeyman" buyer or contract administrator level.
- o Development and execution of plans to eliminate our formal course of instruction training shortfall of 9,400 courses by the end of FY 86. To date, over 3,500 courses have been completed.
- o Conduct of internal "modular training" for individual buyers and contracting officers when specific knowledge or skill deficiencies are identified through conduct of compliance reviews.

In addition to the above, we have, in the last year, restructured to what we believe is the most efficient organizational structure. We have made progress toward our ultimate objective of removing clerical work from our buyers and contracting officers to elevate them to a status of being professional decision makers and problem solvers. We are attempting to improve morale by providing better working conditions for our employees. These initiatives are expected to produce positive paybacks in increased productivity of our contracting and contract management workforce. We also expect a concommitant improvement in the quality of the work they produce.

STATUS OF IMPLEMENTATION OF THE 1984 DEFENSE PROCUREMENT LEGISLATION AND ITS IMPACT

GENERAL

The primary thrust of the 1984 defense acquisition legislation was to reform the outdated Armed Services Procurement Act of 1947 and effect competition and pricing improvements. The legislation, for the most part, accomplishes that purpose and we support it. The legislation did not eliminate some statutory requirements applicable to small purchases. It added other requirements which present, or are expected to present, what I believe is an unnecessary burden with minimal to negative payback and which thwart any management initiatives to contain or reverse leadtime increases.

THE COMPETITION IN CONTRACTING ACT OF 1984

The Competition in Contracting Act of 1984 represented the most significant revision to the Armed Services Procurement Act since its passage in 1947. Its implementation, therefore, resulted in a major revision of the Federal Acquisition Regulation and the DoD FAR Supplement, the two principal acquisition regulations under which we operate. Those revisions were made on such a timely basis, that we were able to revise and issue a complete new edition of our DLA supplementary contracting guidance, the Defense Logistics Acquisition Regulation, on 13 February 1985 - well in advance of the statutory implementation date of 1 April 1985. The advance placement of the regulations needed by our contracting, legal and logistics personnel to accomplish the conversion to CICA's provisions allowed our field activities to make that conversion to the new contracting policy concepts in a timely manner.

To further ease the conversion to CICA's new acquisition policy requirements, we developed and conducted one-day seminars on the new statutory and regulatory requirements for contracting, legal and logistics personnel for all of our procuring activities. We trained approximately 4,000 personnel in 33 separate sessions during the period 11 February 1985 through 28 March 1985.

As a result of having the regulations in place well in advance of the 1 April 1985 implementation date and the conduct of familiarization training, our conversion to CICA was accomplished on time, with minimal disruption of operations and with what we believe was significant cost avoidance. DLA procuring activities began issuing solicitations under the new requirements on 1 April 1985.

We implemented the protest provisions of the Act as of 15 January 1985. We did, however, on advice from the Department of Justice, along with the rest of DoD, refrain from implementing the "stay" provisions of the new 10 U.S.C. 3553(c) and (d) relative to General Accounting Office (GAO) bid protests. Based on subsequent court decision and Department of Defense implementation of these provisions, we implemented those provisions of the law in July 1985.

We implemented the expanded procurement notices (synopsis) requirements of CICA and the Small Business and Federal Procurement Competition Enhancement Act on 1 April 1985. There were some delays on particular acquisitions caused by obtaining the additional descriptive data of the item of supply being acquired to satisfy the new requirements for publication of an item's form, fit and function and material of manufacture. As of now, however, when we have descriptive data which is releaseable to the public, we are publishing it in the Commerce Business Daily.

We now have activity Competition Advocates at all of our procuring activities and contract administration services regions. We have also designated an Agency Senior Procurement Executive and an Agency Competition Advocate, both of whom are at the general officer level.

THE DEFENSE PROCUREMENT REFORM ACT OF 1984

The majority of the provisions of the Defense Procurement Reform Act of 1984, which is applicable to DoD alone, are also contained in the Small Business and Federal Procurement Competition Enhancement Act of 1984 as being applicable to the civilian agencies. Those provisions are being implemented on a Government-wide basis. They have either just recently been implemented or have just recently been approved for publication in the Government-wide Federal Acquisition Regulation. Considering the time it takes to place and complete contracts, it will take a minimum of at least another year to assess the impact of a number of these statutory provisions.

We had regulatory coverage similar to a few of the Act's provisions prior to its enactment. We do have experience, therefore, with some provisions of the Defense Procurement Reform Act which parallel ours. For example, the Act requires supply contractors to identify the manufacturing source and to provide item identification. We have been including a provision to obtain similar information in all of our part numbered spare parts solicitations since 1968. DLA's solicitation provision requires source identification of the product offered as part of an offer. That provision has two principal purposes: (1) to allow for evaluation of alternate offers for part numbered items, thereby providing opportunities to expand the competitive base; and (2) to assure that the item of supply for which we contract is an acceptable alternate to the item described in the solicitation. We will subsequently solicit offers from both approved parts manufacturers and original equipment manufacturers of all of the approved part numbers. It is not always possible, however, to accept the part from the parts manufacturer directly. This is because value, in the form of finishing operations, functional testing of assembled parts, detailed receipt inspection, and warranty protection, which assure reliability of the part, is sometimes added by the original equipment manufacturer. Use of this provision has increased competition for spare parts over the course of several years.

The Act contains other provisions requiring solicitation of economic order quantities. Our small purchases include a provision inviting quotes on a more economical quantity. In addition, our Supply Centers have implementing procedures for large purchases which provide for solicitation of several alternate quantity ranges, when it is practicable to do so. When those quantity/price range offers are received, a decision is made, based on stock and usage requirements, as to whether a different quantity from the principal one solicited should be acquired. Use of such provisions frequently results in the purchase of more economical quantities.

The Act also requires item descriptions to be sufficient for buyers to be knowledgeable of what they are buying. The purpose of this provision is to allow buyers to have an idea of how much an item should cost. The actions we have taken to implement this provision of the law include the following:

- o Conduct of technical review of items prior to procurement to assure sufficient item description.
- o When a sufficient item description is not available, we ask the requisitioner and/or manufacturer for part number verification and item description.

- o When available, we provide the buyer with a picture or graphic of the item. We are currently exploring various alternatives for obtaining pictures for unique items or those with insufficient descriptions.

The Act contains other provisions for front end planning for major systems. These provisions are applicable to the military department that is developing the system. We will not begin to experience the effects of these provisions of the Act until we begin to support those systems approved, following the development stage, for full scale production.

The Defense Procurement Reform Act also provides DoD authority to waive contracting requirements for petroleum acquisitions under extraordinary adverse market conditions. Acquisition of petroleum products for the Department of Defense is a major DLA program. The regulatory provisions implementing the Act's authority will be in place shortly. The Secretary of Defense has delegated this waiver authority to the Assistant Secretary of Defense (Acquisition and Logistics). We believe that this authority will significantly improve our ability to satisfy the Government's petroleum requirements when we are faced with severe adverse petroleum market conditions.

The Defense Procurement Reform Act further requires that we establish performance appraisal systems which give recognition to efforts to increase competition and achieve cost savings in contracting. We are doing that, where appropriate. Standardized performance standards for our buyers and contracting officers have been developed and are currently being implemented. Changes to current performance standards to incorporate competition for our senior contract management personnel are also either under development or in place. As an example, one of the critical elements against which performance is measured for our buyers is whether awards are consistently recommended at a fair and reasonable price considering the complexity of each buy, nature of the item, competitive base, and urgency of the requirement.

THE SMALL BUSINESS AND FEDERAL PROCUREMENT COMPETITION ENHANCEMENT ACT OF 1984

The Small Business and Federal Procurement Competition Enhancement Act requires the Small Business Administration (SBA) to assign Breakout Procurement Center Representatives and technical advisors at major procurement centers. The SBA has, thus far, assigned Breakout Procurement Center Representatives or their technical advisors at all of our Hardware Centers. SBA has elected to service our other two Supply Centers on a liason basis. We do not, as yet, have sufficient experience with their efforts to provide a meaningful assessment of their effect. We are working to assure that they accomplish their intended function and that their efforts are compatible with those of our Activity Competition Advocates.

GENERAL ASSESSMENT OF THE IMPACT OF THE STATUTORY COMPETITION AND PRICING REFORMS

Most of the matters I have just addressed have had or are expected to have a beneficial effect on our efforts to enhance competition and improve the quality of our contracts. We expect to continue to experience positive paybacks from increasing competition, but not at the same rate or to the degree we have experienced them in the past two years or so.

As I mentioned earlier, the following provisions are hampering us from achieving further economy and efficiency in the process of placing contracts.

CERTIFICATE OF COMPETENCY

The Small Business and Federal Procurement Competition Enhancement Act of 1984 requires the Small Business Administration to process certificate of competency (CoC) actions on all determinations of nonresponsibility of a small business, regardless of purchase dollar value. Historically, the contracting officer has made the decision as to the responsibility of a small business firm for small purchases. Now, this decision rests with the SBA when we determine a small business offeror on a small purchase to be nonresponsible.

If future experience parallels our recent past experience, compliance with the requirement to refer small business nonresponsibility determinations against small purchases to SBA for CoC consideration could result in up to 33,000 additional referrals annually to SBA from DLA alone. In FY 84, when this requirement applied only to large purchases, we referred only 417 nonresponsibility determinations to SBA. DLA's FY 85 average small purchase dollar value was $1,702. The additional leadtime involved in such referrals is 45 to 90 days, depending on whether a preaward survey is conducted and on whether the contracting officer elects to appeal a decision to issue a CoC. Such referrals require additional manpower resources to be expended on the part of SBA, the contracting officer, and the Defense Contract Administration Services. Further, it cannot be precisely known which procurements will result in a requirement for CoC referral until offers are received and evaluated. This uncertainty hampers our ability to assure that sufficient stocks are on hand at all times to satisfy requirements to assure military readiness capability.

Currently, by statute, all purchases valued under $10,000 are reserved for small businesses. Further, a significant number of purchases valued between $10,000 and $25,000 are set aside for small businesses. As a result, when we do find the low small business concern nonresponsible, an overwhelming majority of resulting awards are made to the second low responsible small business concern. The result of this legislative requirement will, therefore, be substantial administrative effort which will not appreciably increase the number of awards to small businesses.

DLA is strongly committed to the small business program. Our performance in this area clearly reflects this strong commitment. We question whether the small business program is well-served by contracting with offerors we have determined are not responsible, particularly when the next low offeror is a responsible small business. Further, it diffuses responsibility in assuring that contracts are awarded only to responsible offerors. The procuring activity is charged with obtaining quality supplies timely, yet cannot assure that result themselves.

OTHER REQUIREMENTS

The Defense Procurement Reform Act of 1984 and the Small Business and Federal Procurement Competition Enhancement Act of 1984 did not change the synopsis threshold. It remains at $10,000, in spite of the fact that Congress raised the small purchase threshold to $25,000 for DoD in 1981 and for the civilian agencies in 1984. Further, no change was made to the small purchase-small business reservation threshold. It remains applicable to purchases valued under $10,000.

We thus have three levels of buys, rather than just the two, large and small, we had before the small purchase threshold was raised. We cannot process purchases valued between $10,000 and $25,000 through our competitive automated small purchase system. This is because we have to synopsize those purchases and because a set-aside determination must be made on them. The result of these disparities in the law is an increased potential for spending more to place a contract than the item being bought is worth.

Attached to this statement is a list of recent statutory requirements applicable to the three purchase thresholds: $0 to $10,000; $10,000 to $25,000; and $25,000 and above. In general, that attachment shows that implementation of recent statutes has added considerable leadtime to all purchases. The attachment shows that all the selected statutory requirements which apply to large purchases valued $25,000 and above, except for the cost or pricing data requirements, also apply to small purchases in the $10,000 to $25,000 range. Clearly, the attempt, in the Competition Contracting Act, to permit simplified small purchases has not been achieved.

Further simplification of small purchases could be achieved by: application of a uniform definition of a small business - that definition which is now applicable to small business set-aside acquisitions; and rationalization of various socio-economic thresholds to application at the $25,000 and above level. Effecting these changes would eliminate administrative burdens which have insufficient benefits to warrant them. These changes would also allow us to make greater use of existing automated small purchase systems for competitive items, thereby providing for further economy and efficiency in the cost of placing contracts. This would allow our buyers to concentrate on the "problem" buys.

We have gained some experience with the Competition in Contracting Act's requirement to provide for full and open competition. Based on that experience, it appears appropriate to evaluate that concept. We should assess the costs of that concept against the returns in savings and cost avoidance. A concept of adequate and effective competition may be the most logical alternative.

The Defense Procurement Reform Act of 1984 provides that an offeror may not be denied the opportunity to have its offer considered solely because the offeror is not on a qualified bidders, manufacturers or products list. These tools can be used to both reduce administrative leadtime and improve the quality of products. The latitude to require such qualification by the time of solicitation closing would allow us to achieve the objective of qualification processes.

SUMMARY

Significant benefits have resulted from the recent procurement reform legislation, including increased competition with resulting contract price savings. However, these benefits have not been obtained without cost in terms of increased leadtime, decreased supply availability, and increased manpower requirements due to declining contracting workforce productivity. Further refinements would overcome some of our problems.

In the future, may I propose that the Subcommittee consider, when proposing new legislation which could significantly affect our operations, conducting a test of such changes on a limited basis. From such a test, we could assess the positive and negative effects of such changes, before implementing them on a DoD-wide basis.

I would welcome the opportunity to work with all of you to obtain the refinements which are necessary to accomplish these improvements.

ATTACHMENT

Procurement Administrative Lead Time and Production Leadtime

Resulting from Statutory Requirements

Small Purchases
($0-$10,000)

DLA Activities Affected	Legislative Requirement	Number of Days Leadtime
Hardware Centers (primarily)	DoD Authorization Act of 1985 - buyers must know what they are buying	3, if data in house 14 - 90, if data not in house
All DLA Activities	P.L. 98-577, CoC referral to SBA required for all nonresponsibility determinations against a small business	45 - 90 (when applicable)
Hardware Centers	DoD Authorization Act of 1984 required certification to Head of Contracting Activity (HCA) for spare parts price increases of 25 percent or more	1 - 2 (when applicable)
All DLA Activities	Competition in Contracting Act of 1984 instituted "stay" provisions on GAO protests filed within 10 days of award	2 - 115 days after award (when applicable)

Small Purchases
($10,000 - $25,000)

DLA Activities Affected	Legislative Requirement	Number of Days Leadtime
All DLA Activities	Small Business Act and Office of Federal Procurement Policy Act-solicitation cannot be issued until synopsis published (Federal Acquisition Regulation (FAR) establishes presumptive transmittal time of synopsis to Commerce Business Daily (CBD) to assure compliance with statute)	6, electronic - 10, mail (old - 2 days and 5 days, respectively) (gain - 4 days and 5 days, respectively)
All DLA Activities	Small Business Act and Office of Federal Procurement Policy Act require synopsis before solicitation issued	15 (old - 10 days) (gain - 5 days)
All DLA Activities	Small Business Act and Office of Federal Procurement Policy Act require minimum response time	30 (old - 20 days (commercial items) or 30 days (noncommercial items)) (gain - 10 days)
Hardware Centers	DoD Authorization Act of 1985 - buyers must know what they are buying	3, if data in house 14 - 90, if data not in house
All DLA Activities	P.L. 98-577, CoC referral to SBA required for all nonresponsibility determinations against a small business	45 - 90 (when applicable)

Small Purchases ($10,000 - $25,000) continued

DLA Activities Affected	Legislative Requirement	Number of Days Leadtime
Hardware Centers	DoD Authorization Act of 1984 required certification to HCA for spare parts price increases of 25 percent or more	1 - 2 (when applicable)
All DLA Activities	Competition in Contracting Act instituted "stay" provisions on GAO protests filed within 10 days of award	2 - 115 days after award (when applicable)
Hardware Centers (primarily)	P.L. 98-577, expanded synopsis requirements	0 - 2 (one time)
All DLA Activities	Small Business Act requires small business set-aside determination	0 - 2 days

Large Purchases ($25,000 and above)

DLA Activities Affected	Legislative Requirement	Number of Days Leadtime
All DLA Activities	Small Business Act and Office of Federal Procurement Policy Act - solicitation cannot be issued until synopsis published (FAR establishes presumptive transmittal time of synopsis to CBD to assure compliance with statute)	6, electronic - 10, mail (old - 2 days and 5 days, respectively) (gain- 4 days and 5 days, respectively)
All DLA Activities	Small Business Act and Office of Federal Procurement Policy Act - require synopsis before solicitation issued	15 (old - 10 days) (gain - 5 days)

Large Purchases
($25,000 and above) continued

DLA Activities Affected	Legislative Requirement	Number of Days Leadtime
All DLA Activities	Small Business Act and Office of Federal Procurment Policy Act - require minimum response time	30 (old - 20 days (commercial items) or 30 days (noncommercial items)) (gain - 10 days)
Hardware (primarily)	DoD Authorization Act for 1985 - buyers must know what they are buying	3, if data in house 14 - 90, if data not in house
All DLA Activities	Small Business Act requires referral to SBA for CoC consideration of nonresponsibility determinations against a small business	45 - 90 (when applicable)
Hardware Centers	DoD Authorization Act for 1984 required certification to HCA for spare parts price increases of 25 percent or more	1 - 2 (when applicable)
All DLA Activities	CICA instituted "stay" provisions on GAO protest filed within 10 days of award	2 - 115 days after award (when applicable)
Hardware (primarily)	P.L. 98-577, expanded synopsis requirements	0 - 2 (one time)
All DLA Activities	Small Business Act requires small business set-aside determination	0 - 2 days
All DLA Activities	Competition in Contracting Act lowered cost or pricing threshold from $500,000 to $100,000	30 - 60 days (when applicable)

Senator **Quayle**. Thank you very much, gentlemen.

If I could summarize, I detect what you are saying is that the general interest and, the general thrust of the recent procurement legislation has been in the right direction. We have emphasized competition. We have emphasized getting small businesses and more people doing business with the Department of Defense.

On the whole, the thrust seems to be in the right direction. But then it stops and I hear you say that is right, but for a few things. It is like everybody is for cutting spending here, but for my particular program.

We have been in that trap before; we are for it, but for this. What I am trying to do is get the "but for" that you have on your mind.

I was listening to your testimony and I think that a couple were specifically mentioned in the CICA provision. I know that General O'Loughlin paid particular attention to the stop-work provision and the protests that are filed with GAO and also the definition, I think General Thompson and General Skantze also mentioned this, concerning the full and open competition versus adequate competition.

General Babers, you pointed out, I think, a Small Business requirement, the certificate of compentency, and how many additional people in the Department it is going to require.

Does anybody else want to come forth with some of the specifics in the procurement legislation, I want to set aside your concern, General Skantze, with FOIA, right now, because I want to get into this issue where we discuss the personnel system within procurements. Are there a couple of other specifics in this piece of legislation that you would like to put a "but for" stamp upon?

General **Skantze**. Maybe it is a little parochial on my part, but one of the things that we did not mention, but is pending in legislation, is the idea of providing work measurement data to the Congress.

I think this is at least a recommended amendment that Senator Grassley and Miss Boxer both propose.

First of all, the entire work measurement area is a very complex kind of standard to deal with in what is work efficiency and how you use these standards to do pricing in competition and the fact that when you start in with new technology and new development it takes you a while to develop the standards because the first thing you have to figure out is what are you going to build and how complex it is to build.

So that real standards do not come to pass until you have gotten well into production and all of the turbulence and changes and everything else has matured. So, people who are good industrial engineers and understand that process know how to put those together.

We use them and we put them on contract, but if there is a mandate that says the standards have to be used for all pricing, some of the standards are not even developed for programs that are in embryonic stages of full-scale development, the concern was that if we have to do that and provide all this data to the Congress as the amendment currently stands, it is confusing.

I think we would have an enormous workload in just generating all that information which may or may not be applicable to the particular contract, but would be mandated.

Now, that has not come to pass, but it was one of the proposals to the authorization conference.

Senator **QUAYLE**. Assuming that the authorization bill passes in the House and in fact will become law, we will add the work measurement standards.

Does anybody else have some candid thoughts?

General **O'LOUGHLIN**. I would like to see the bid package requirements. We spend an inordinate amount of money on bid packages. Every vendor who wants to solicit can get one.

I can cite you specific cases where we have had as many as 500 bid packages on an item of less than a $10,000 contract and maybe get two bids back. Those bid packages can run from $5 to $10 to $15 to $40 or more per bid package depending on the amount of engineering information, the kind of data we have to provide.

Senator **DIXON**. Of course, you charge for that, General?

General **O'LOUGHLIN**. We can charge for it, but we have been limited to do that by our services.

Senator **DIXON**. The law permits you to charge for it?

General **O'LOUGHLIN**. Yes; if we can even get a restriction or fix the limits to 10 vendors for small purchases under $25,000 and 25 vendors for purchases over $25,000, it would help us a bit.

Senator **LEVIN**. Which 10?

General **O'LOUGHLIN**. Ten competent. We have enough bidders that we know who are competent and who are capable.

Senator **LEVIN**. The ones who are incompetent do not get the bid package?

General **O'LOUGHLIN**. That is right. First come, first served. We rotate the bidder's list, if necessary.

In addition to that, we would exclude the Debt Collection Act from the Government contracts.

Senator **QUAYLE**. The Debt Collection Act? Why? Why would you want to do that?

General **O'LOUGHLIN**. Let me refer to Gen. Richard D. Smith, my Director of Procurement.

General **SMITH**. It is designed for collection of debts from individuals in a commercial environment. Previously we received consideration from a company when a company owed us.

Now we cannot offset what they owe us. We have to go through a notification process and go through a full legal process to enforce the Debt Collection Act. It is just another administrative nightmare.

Senator **QUAYLE**. Any other candid views?

Admiral **HUGHES**. We really need a threshold in the requirement for the certificate of competency. I would suggest a $25,000 level because it is parallel to our $25,000 level which requires competition advocates to review.

General **THOMPSON**. Raising the synopsis threshold from $10,000 to $25,000 would also be helpful and we have talked about. There are however, some other thresholds we should look at, such as the Davis-Bacon Act, service contracts, employment of handicapped and others including, as we have mentioned, the certificate of competency threshold.

I think we can offset any impact on small business if we also raise the small-business, small-purchase set-aside threshold from $10,000 to $25,000.

Of course, one other recommendation is to lift the requirement to synopsize 15 days prior to the issuance of a solicitation. We have some numbers on that requirement and it is costing us 11 days in leadtime.

Those are some additional things I ask you to consider.

Senator QUAYLE. These are all candidates for discussion which we are delighted to have.

Do you have any others you want to add?

General SKANTZE. Let me add one more.

Senator QUAYLE. I want to get everything on the table so that we know where to start.

General SKANTZE. CICA mandates justification and approval for solicitations over $10 million will be reserved to the senior executive acquisition agent which in my case would be at the Secretary of Air Force level as opposed to the head of contracting authority.

I suggest that that be removed and allow us to handle those approvals as the heads of contracting authority because thus far any we have sent forward have not been denied. It raises us to an unnecessarily high level.

Senator LEVIN. Sole source?

General SKANTZE. Yes.

General O'LOUGHLIN. I think we maybe ought to get together and submit you a list of these kinds of things.

Senator QUAYLE. I hoped you would come forth with those in your testimony. If you want some more time to come up with some specifics——

General O'LOUGHLIN. They are in the basic testimony.

Senator QUAYLE. We will be glad to keep the record open a little bit to have additional testimony. What we really need to have are things that cause you problems and the documentation so that we can begin a discussion about it. That is what oversight is all about.

[Additional information follows:]

STATUTORY PROVISIONS WHICH SHOULD BE REPEALED OR MODIFIED

Admiral HUGHES. In addition to those statutory problems already covered within this hearing, we would like to address P.L. 95-507 and the mandatory small business subcontracting plans in contracts over $500,000. Navy's implementation has not been without cost, and expenditure of time by the contracting work force continues.

Administrative effort can be reduced, and at the same time, we can enhance the effectiveness of the subcontracting program, by making a few changes:

We could be more successful in achieving our purpose by negotiating and approving master subcontracting plans with goals on a corporate, company, or subdivision basis rather than the individual subcontract plans currently required. By eliminating subcontracting plans for thousands of individual Federal contracts awarded each year, more effort could be devoted by the government and the prime contractor to ensuring compliance and monitoring effectiveness.

Master plans should be approved by the cognizant contract administration office and reviewed by the SBA since these two entities already have the responsibility for monitoring, evaluating, and documenting a contractor's performance, and have the "corporate" knowledge and experience to know if the contractor is satisfactorily carrying out the subcontract provisions of a particular prime's contract. Further, they are in a better position to take corrective action, if necessary, and have better leverage in achieving the desired results than if the responsibility remains fragmented among individual contracting officers.

The term for these master subcontracting plans could be extended to cover a period of up to three years as determined on a case-by-case basis, reducing the burden created by annual renegotiation of these plans for those contractors whose line of work does not significantly change over time or who demonstrate a solid record of continuously improving performance.

General **Skantze**. I would like to raise several other issues. Current warranty legislation under P.L. 98-525 limits our available acquisition strategies and increases costs. Warranties are but one tool considered during the development of an acquisition strategy to attain our performance and supportability objectives. It does not make sense to require warranties for many satellite and missile systems. We clearly need increased flexibility; therefore, I strongly recommend that warranty waiver authority be vested in the Head of the Contracting Activity and that performance incentives be used in lieu of warranties when appropriate.

Additionally, the ability of our field people to "break-out" components, subsystems, support equipment, etc., is seriously hampered if the value is in excess of $10M. Competition in Contracting Act requires a new Justification and Approval if we are unable to compete. The law should be amended to allow break-outs when the data is not yet available for competition Clearly, a "class type Justification and Approval" or an 8th exception should be incorporated into P.L. 98-369 to facilitate early break-out of spares and support equipment.

General **O'Loughlin**. Specific recommendations are addressed in the basic testimony. With specific regard to sole source approval levels for AFLC, the Commander should have unlimited approval authority. The provisions in the fiscal year 1986 DOD Authorization Act are separately addressed.

Senator **Quayle**. Now I would like to get a general feeling from you on your allocation of resources in response to procurement legislation.

Dr. Wade was before this subcommittee last week in opening these hearings. He talked about quality assurance and quality should be top priority. Now, with the legislation and also with any of the other regulations within the services, where is the allocation of resources going in personnel?

Is it going to quality assurance? Is it going to procurement, spare parts, competition? What are you doing in your allocation of resources?

General **Skantze**. In my case it is all of the above because I created the Deputy Chief of Staff for Product Assurance which covers quality and many other things. We have painfully stripped our people from other functions and put more into the quality engineering function, particularly at the product division and Air Force plant rep level.

In addition to that, we did get some increases over the past couple of years in people in the procurement business. These are new hires. In our case it was about 750. Those people are in place. They are still going through the maturation cycle, if you will, and I suppose the thing that burdens our process, at least in my mind, is our people are very, very, very cautious about what they do.

They are afraid that they will be fingered as having made an award or cost estimate or negotiated without sufficient data. So, the process of getting more data from the contractor to be absolutely 100 percent certain that you cannot become the subject of a horror story or a hot-line call on abuse has tended to create a degree of ultraconservatism in the work force where it is stretching out the process.

I cannot stress too much that the Government work force, in my case, the command, has 53,000 people and about 20,000 full time in procurement, and they have just gone through a couple of years of listening to themselves maligned and as a result, we have lost some very good ones, but those ones who are staying, you know, are in many cases, the right word is, deathly afraid to make a mistake.

Senator QUAYLE. General O'Loughlin?

General O'LOUGHLIN. I second what General Skantze says. We in AFLC, even though we have 97,000 people, handled $54 million last year. We added 1,480 people to our competition advocacy role and another thousand people to a combination of procurement and material management.

The mind-set I spoke of in the austere years of watching what you spend and the raising inflation and when you get to pay the bill, you could not pay the bill, basically, we have a lot of mind-set that we are trying to work out that way.

We have had good training programs now. The recruiting is going very well in the Pacer Produce I and Pacer Produce II, which are programs to put qualified people into the competition advocacy role and procurement ninety percent of our new hires have a bachelor or master degrees. That is now starting to pay off.

I would not be honest with you if I did not tell you that at the end of the fiscal year, along about September 30, we had a lot of zombies walking around procurement because they had worked overtime 7 days a week for the last 2 months.

The same syndrome that General Skantze talked about in regard trying not to make a mistake permeates the organization. This is due to all of the adverse publicity.

Senator QUAYLE. This is my last question and then I will yield to Senator Levin.

General Skantze, I think a couple of others have hit upon the careers of procurement officers and the problem of getting better procurement management.

Do you think it is time for us, particularly with regard to the civil service to look at an alternative civil service system for the military, an alternative civil service system that would probably have a different way of promotion, to get people in engineering, technology, let's leave the military aside because we concentrated on that a bit in the last legislation, but rather at an alternative civil service system. Do you think it is a good idea and, if so, very quickly, what should we be searching for in this area?

General SKANTZE. I do not think at the moment I can comment on an alternative civil service system, but, obviously, our problem is that we are competing for very qualified kinds of people in the procurement process as well as our engineers.

We have plants and organizations in very highly competitive areas like Los Angeles, San Diego, and Palo Alto, where because of the grade structure and salary and sort of the nonprofessional aspects of procurement, we do not compete very well and when we do get people, as soon as we get them trained, we lose a lot of them to industry.

So, something needs to be done to fundamentally correct that process. Whether it is an alternative to civil service, I do not know.

General THOMPSON. I am not so sure whether or not I am talking about an alternative system, but it is something that needs to be fixed considering the way it is run today. Let me give you an example.

I should be looking for in the procurement process for an individual, for example, who can negotiate. That is a very particular kind of skill. In order to get an individual at an appropriate grade level, he must supervise a certain number of people who in turn must supervise a certain number of people. That does not make sense. That kind of thing requires looking at.

Senator **Quayle**. Admiral Hughes?

Admiral **Hughes**. First of all, in answer to your first question, we have concentrated a lot of our additional people in the pricing problem vis-a-vis the overall acquisition.

In our project, BOSS, we have between 700 and 800 people looking at that. We have upward of 150 to 200 people in the competition advocacy program. I think we really need to put more billets to cover added training requirements and keep a pipeline going—an internship—type program.

To address the civil service issue, on the 20th of July the Deputy Secretary of Defense went to OPM and asked for some, I guess I would say some leniency in the approach to classifying procurement people.

The response we got, I think, missed the point to a significant extent. The idea that Mr. Taft had was that the system has changed and the response we got essentially said: Gee, we just overhauled it in 1983 and we broadened the coverage to GS-15 from GS-12 and GS-13.

Well, the system has changed since 1983. Pressures have been very great during that period of time. I think that was overlooked in the response.

We have what we call a demonstration project in the Navy out at China Lake—we had it in two places, but I forget the other place—where management is given a leeway in the range of salaries by relating them to performance and productivity. He is allowed to move them up vis-a-vis a strict classification range. He is doing that for engineers principally.

That could be expanded to procurement. Our experience, and we have been criticized for it, over the 3 or 4 years we have had this in being, maybe close to 5, is that our costs have gone up between 5 and 6 percent. It has been a percent a year increase in cost.

I do not think it is a heck of a lot more to end up paying for the added talent we are looking for.

General **Babers**. I think we have a major problem the way we have managed the acquisition work force right now. I do not know if it needs surgery or some other cure, but something of the type of cure you described should be strongly considered before it is discarded.

Senator **Quayle**. Gentleman, thank you.

The two questions that Chairman Goldwater wanted me to ask were:

One, he wanted you to submit for the record the number of reports and the pages that you have had to respond to Congress.

He also wanted to know items that you consider that Congress has added over the years in the area of micromanagement.

If you can give us those two little things, he will be greatly appreciative.

[The information follows:]

The information requested is not routinely gathered or maintained by the Department and therefore had to be reconstructed using the latest data available. In this case, we selected fiscal year 1985 wherein we identified 458 congressional reporting requirements stemming from the Defense Authorization and Appropriation Bills and their accompanying reports. Of that number, approximately 390 or 85% have been furnished with the balance either currently being worked or contingent upon an event occuring to trigger its being required. Based on this we estimate about 24,000 pages have been submitted in connection with these requirements.

General SKANTZE. It is not possible in the time allotted and given the amount of resources available to determine the number of reports and pages submitted to Congress during the past year. However, a review of the FY 86 Authorization Bill reveals that an additional 107 reports will be required to be submitted to Congress. This is an example of Congressional micromanagement of the DOD acquisition activities.

Congessional micromanagement of DOD acquisition activities occurs when legal legislation goes beyond broad policy guidance and invokes specific requirements affecting individual contract and program management actions. Congress should enact broad policy and allow implementation of this policy through the DOD regulatory process. The DOD must maintain flexible management authority in order to implement Congressional policy in the most efficient and cost-effective manner. When management's flexibility is inhibited by legislative action, systemmatic inefficiencies can occur. The following are examples of legislative actions which go beyond broad policy guidance:

1. Section 917 in the FY 86 Authorization Act, "Cost and Price Management in Defense Procurement." This legislation requires DOD to develop a new system to record actual, negotiated, and proposed costs on all contracts over $100,000 that require cost and pricing data. Also, contractors are required to maintain records comparing their projected labor costs with "standard time allowances" for comparable work in commercial industry. This is an example of Congressional micromanagement because it involves specific reporting requirements in a very technical functional area. Since the basic premise and technical content of the proposed law is flawed, the Congress is subjecting itself to wrong conclusions about defense contractor efficiency.

2. 10 USC 2403, Weapon System Warranties. The law requires the following warranty coverages on every weapon system production contract: conformance to design and manufacturing specifications, freedom from all defects in materials and workmanship, and conformance to essential performance requirements. These specific coverages are not always applicable to weapon systems. For example, remedies to correct defects in materials and workmanship cannot be invoked once a satellite is deployed. Conformance to essential performance requirements cannot be tested for dormant systems such as GBU-15 or Peacekeeper Propulsion Stages. Congress, by defining specific requirements in legislation, has inhibited management authority. When a warranty does not make sense, the Program Manager must obtain agency head approval to waive the warranty requirement. The agency head is further constrained by having to notify Congress on a case-by-case basis of all waivers. This delays the acquisition process by a minimum of 30-days.

3. Section 912 in the FY 86 Authorization Act, "Multiple Sources for Major Defense Acquisition Programs." This legislation requires the Secretary of Defense (SECDEF) to submit to Congress an acquisition strategy plan for all major programs entering full-scale development. The SECDEF shall provide at least two sources for FSED and production unless it would materially increase program costs or unreasonably delay completion of the total program. This waiver authority by the SECDEF is only valid up to 50% (dollar value) of the total cost on all major development and production programs. This legislation is micromanagement because it legislates specific program management requirements which should be an independent decision on a program-by-program basis. The existing acquisition system properly addresses dual sourcing objectives. Analysis and program management action is the proper way to address this issue. These legislated constraints add an undue burden, given the already extended acquisition cycle and limited resources.

4. Section 913 in the FY 86 Authorization Act, "Minimum Percentage of Competitive Procurements." This legislation requires the Secretary of Defense to establish annual dollar goals for the award of competitive defense procurement and to submit an annual report to Congress proposing means for promoting and expanding compe-

tition. The Air Force and other DOD components have aggressive Competition Advocate programs designed to promote competition wherever possible. Goals are established and the tracking of results is a continuous activity. There is no need for adding another layer of reporting and competition management. Congress can obtain this data at any time.

5. Section 925 in the FY 86 Authorization Act, "Assignment of Principal Contracting Officers." This legislation requires the Secretary of Defense to develop a policy regarding mobility and regular rotation of Principle Administrative Contracting officers and Corporate Administrative Contracting Officers and to provide a report to Congress by January 1986 explaining this policy. Congress practices in micromanagement when it involves itself in the placement of individuals at the working level. The Air Force has an effective discretionary mobility policy which ensures the Government's interest, as well as, the individual's interests are addressed. A mandatory and arbitrary rotation policy is unnecessary and counterproductive due to personnel limitations and contraints. The Congress should enact policy mandating effective use of personnel, not mandating specific employee rotation practices.

Admiral Hughes. The Congress has, over the years, become more deeply involved in micromanagement of the defense effort, including procurement. Some of this results from the increased number of committees involved, accompanied by a very substantial increase in congressional staff members.

In 1975, four Congressional committees wrote Defense legislation. Today, there are 24 committees and 40 subcommittees involved. Over the last two years, Defense procurement has received concentrated attention. Thousands of pages of testimony have been taken by an assortment of House and Senate committees and subcommittees. This resulted in a wide range of legislation, generating more regulations to be followed by the Department of Defense (DOD) and our contractors.

More important than the volume of legislative requirements is the detail involved. For instance, the pending Fiscal Year 1986 Authorization Bill gives a specific percentage of work to be accomplished on certain contracts before progress payments can be made, specifies the categories in which contract costs shall be collected, requires current industrial standards for bills of labor and material even when there are no standards or standards that can replace effective negotiation, and prohibits contracting out for specific DOD functions, whether or not such prohibition is in the best interest of the DOD and would be cost-effective.

We consider the procurement process as one of the most highly regulated systems in existence. Those who must work with the system daily, both within the DOD and industry, deserve some respite from continued additions to the system as we absorb last year's legislated requirements (Competition in Contracting Act, weapon system warranties, technical data management, breakout procurement center representatives, etc.).

General Thompson. I believe it is fair to say that micro-management has been added at all levels of the acquisition process beginning with the smallest repetitively purchased part to the largest development project. This increase in micro-management is evidenced by the increase in the number of committees, subcommittees and Congressional staff involved in review and revision of the acquisition process and further by the increase in investigative reviews, data calls, testimony and legislation devoted to the procurement/acquisition process. More important is the level of detail provided in recent statutory changes. This level of detail is reflected, for example, in the CICA coverage which sets statutory requirements for what must be included in justifications, for noncompetitive procurements, who should certify to the justification and specific levels for approval applicable to all DOD buying activities without regard to the size or expertise of the individual purchasing activity. Other areas of increased micro-management are reflected in multiyear, warranty, cost and pricing and contract financing arenas to name a few. The major area evidencing micro-management perceived or real, is the area of responsibility. The approach being taken to solve the "ills" of the past is a clear move to centralization of authority and thus responsibility at progressively higher levels.

General Babers. The following are examples of statutory requirements which DLA considers to be in the area of micromanagement:

LIST OF ITEMS CONGRESS HAS ADDED IN THE AREA OF MICROMANAGEMENT

United States Code, description: 10 U.S.C. 2304(a)(2), When an agency shall solicit sealed bids; 10 U.S.C. 2304(d)(2), Authority of subsection (c)(7) may not be delegated by head of an agency; 10 U.S.C. 2304(f)(1)(B), Approval levels for justification; 10 U.S.C. 2304(f)(2), Specifies when justifications and approvals may be made and specifies exceptions to requirement for justifications, rather than permitting the Secretary to develop these; 10 U.S.C. 2304(f)(3), Specifies the content of justifications; 10 U.S.C. 2305(a)(1)(C), Types of specifications; 10 U.S.C. 2305(a)(2), Factors for evaluation must be included in bids/proposals and solicitations must specify opening/closing date; 10 U.S.C. 2305(b)(3), How sealed bids must be opened and evaluated; 10 U.S.C. 2305(b)(4) (A), (B), (C), (D), How proposals must be evaluated and awarded; 41 U.S.C. 403(8), Definition of responsible source; 41 U.S.C. 416(b), List of what a procurement notice must include; 31 U.S.C. 3553 (d) and (e), Post-award "stay" provision of Procurement Protest System and authority to make determination may not be delegated; 10 U.S.C. 2305 (c), Review availability of item through supply system and review procurement history and item description; 10 U.S.C. 2305(d), Planning for major system; 10 U.S.C. 2317, Personnel evaluation; 10 U.S.C. 2319, Qualification requirements; 10 U.S.C. 2321, Validation of proprietory data restrictions; 10 U.S.C. 2323, Certification of commercial pricing; 10 U.S.C. 2384, Identification of sources of supplies; 10 U.S.C. 2384, a, Economic order quantities; 10 U.S.C. 2402, Limitation on subcontractor sales.

General O'Loughlin. The following items are considered to be areas of micromanagement created by Congress:

The Small Business Act which conferred sole authority for determining a small business' capability to perform (relative to all elements of responsibility) to the Small Business Administration.

Line-item by line-item budget revisions by Congress, particularly the Armed Services Committees. "The fiscal year 1985 budget request had 1890 separate line entries in the various procurement accounts and 897 program elements in the various research and development (R&D) accounts. The House and Senate Armed Services Committees changed 440 or 23 percent of the procurement line entries and 317 or 35 percent of all R&D programs." (from *Defense Organization: The Need for Change*, a staff report to the Committee on Armed Services, United States Senate, 16 October 1985. Page 592).

The requirement to establish Breakout Procurement Center Representatives.

The requirement for DOD to establish minimum education, training, and experience levels for O–7s and above assigned to DOD acquisition commands. Training must include attendance at DSMC (or comparable institution). Experience requires eight years in acquisition, support, or maintenance (two years within AFLC, AFSC, AMC, or NMC). SECAF has waiver authority.

The requirement of DOD to establish a formal introductory training program for personnel overseeing quality in contractor facilities.

The requirement for sole source Justification and Approval for awards in excess of 10 million dollars to be approved by the Senior Procurement executive of each service.

Senator Levin. Mr. Chairman, I think that would be a useful bit of information. I think we also ought to find out from the Defense Department how many reports we receive that we didn't solicit, we received from them that we did not solicit.

[The information follows:]

General Skantze. Air Force Systems Command has not issued any reports to Congress which were not solicited by Congress.

Admiral Hughes. To my knowledge, there have been no unsolicited reports to the Congress from the Navy.

General O'Laughlin. We are not aware of any circumstances under which unsolicited reports have been forwarded to Congress by AFLC.

General Thompson. As I have already indicated, information on the number of reports provided is not maintained, nor is information on the number solicited or unsolicited.

General Babers. The Defense Logistics Agency is aware of no reports it has submitted to Congress which were not requested.

In order to put the reports in context, and I agree we probably are excessive in report requests, I think we ought to get that in the context of the total reports we receive from the Defense Department.

Is it 3 percent? What is it?

If it is a small percentage of the reports we receive, that would put it in a different context. Most of the paper we receive over here is paper that we have requested.

I get the same drift that our chairman does here, that basically you folks feel that we have done more good than bad, that we have helped more than we have hurt in all of the reforms that we have adopted in the last few years, but we have some cleaning up to do, some amendments and improvements that we ought to address.

I do not want to put words in your mouth, but would you all agree that on balance these reforms that we have legislated in the last few years have helped more than they have hurt?

Should we start on a positive note or is that an excessively generous assessment of what Congress has been doing in the last few years?

Would anyone agree with that assessment of the enactments over the last few years, while they have taken time to institutionalize, they have helped more than they have hurt?

General **Skantze**. I would say they have helped more than they have hurt.

At the same time, they have lengthened the process considerably. That is a matter of time and effort and that is money.

Senator **Levin**. That is the hurt part.

In addressing the parts that we have added to the problem instead of the solution, we have solicited from you testimony. The chairman has asked you what should you add to your testimony.

Assume we put together the specific recommendations in your testimony for the record plus what you added orally and emphasized and anything you submit later for the record in the next few days, putting all that together, we will have a pile of particulars as to what changes you would like to see in the reforms that we have adopted or in laws that existed before those changes.

That is the purpose of the hearing that the chairman called and I think it is extremely useful. We have to sift those one by one and go over the pros and cons.

I believe, General, you mentioned the appeal to the GAO, the fact that that halts the process. I remember when I first got here getting a complaint from a constituent who had an appeal to GAO that he expected to win and he did win, but it did not do any good; he won the appeal, but lost the contract. If the contract had been held up during the appeal, he would have won the contract.

In order to have the appeal have some efficacy, you ought to give the person appealing a chance to have some good come from it if he wins.

I understand what you are saying, statistically we stop 99 percent of the work, whatever the figure is, but we also deprive the 1 percent who prevail from gaining the contract that they are appealing the loss of. There are pros and cons on that.

Almost every one of these has trade-offs, as you all know, and in some cases this committee has been instrumental in pursuing the reform. In other cases the subcommittee has been instrumental in stymieing some of the recommended reforms and opposing them that have come on the floor, and come from the House, and we stopped in conference. We have been on both sides.

We have had to weigh trade-offs. We have been on the reforming side. In other cases we have been on the side that it would contribute more to the problem than to the solution. There is a whole bill of particulars that we have to look at, we will compile from your testimony, and so forth.

That raises an intriguing question. General Thompson said that we now ought to institutionalize the changes that we have made to date, the last page of your testimony.

Basically, you all have said let it settle down for a while. We have a lot on our plate. We have got to get this down to the full institution, it takes a couple years to do that, for heaven's sake, let what we have done settle down now before you come up with more changes.

On the other hand, you are proposing more changes, admittedly in a different direction, but nonetheless, changes.

So, my question of anyone who wants to answer is: You want us to now let this thing perk quietly for a few years and, if so, you want to include in that stability process, leaving in place things that you think we ought to change?

Admiral **Hughes**. Mr. Chairman, I think that the items that have been brought up for the most part today for change are not great changes. They are things that are done quite easily. The thing I spoke to, of having a threshold for a certificate of competency, is not a major item; but let me tell you I do not think it is executable the way you have it right now.

You know, making a change like that is establishing a threshold or classification. I do not see that as a big legislative problem.

Senator **Levin**. I know you will hear from Senator Dixon. That was part of a Small Business bill on which he took a leadership effort.

Senator **Dixon**. It was part of the total package. It was a question referred from the Small Business Committee, of which I am a member, and to the Armed Services Committee, of which I am a member.

Senator **Levin**. We faced that in both committees and there was testimony on that issue. I do not think the solution is quite as simple as you suggest.

Many of these reforms are not as simple as they sound. Many of the things that you are proposing have been the subject of hearings and deliberation. I would think that to change them in many instances would require a process of hearings, deliberation, debate, and there would be changes.

They sound easy, but they would be changes. I take it you are saying that you want the system to be left alone basically except for the changes that you are proposing and those you would like us to proceed on even though it violates the more general idea of letting things be stable for a while?

General **Skantze**. I think the changes are designed to, one, take some of the confusion out of the process where we have conflicting statutes on competition, also to take out some of the redundancies where you are going to set up a breakout representative versus the competition advocates which we already have.

It seems to me that when the first warranty law was written, it was recognized very rapidly that it was terribly inflexible and that was amended subsequently quite rapidly without any other changes in that particular statute.

Senator **Levin**. To change the subject for a moment, we received from the Air Force and Navy, I believe, the increases in competition that have taken place over the last few years. I do not know that we got it from the Army orally in your testimony. Perhaps we did.

General **Thompson**. Let me give you the AMC numbers. From 31 percent in 1983, we finished in 1985 with 34 percent.

Senator **Levin**. Thirty-one to 34?

General **Thompson**. Yes, sir.

Senator **Levin**. That is in dollars?

General **Thompson**. That is in dollars. That also reflects the fact that total dollars awarded in 1983 were $18.9 billion and in 1985 were $23.6 billion. We have had similar success.

Senator **Levin**. Have you kept your measurements the same in terms of competition? Can we assume when you compare earlier years to later years, they are the same?

General **Skantze**. They are standard. We negotiated the multiyear B–1B program which generally was generated in a competitive environment with the ATB. If I could have counted $8 billion, we would have had 50 percent in 1985.

General **Thompson**. We also keep it in procurement actions as well as dollars. We have other measures. Sometimes that is a nuance that should be appreciated.

For example, in AMC we went from 48 percent in fiscal year 1983 to 54.6 percent in fiscal year 1985 in the number of competitive procurement actions awarded.

Senator **Levin**. If it is not already in your testimony, I think we ought to have for the record the percentages of procurement actions and dollars over the last 5 years from each of the services in constant measurement.

If you can submit that, it will be helpful to us, and the DLA as well.

[The information follows:]

General **Thompson**. The following information is provided in response to the request for the competition statistics for FY 81–85.

AMC AND ARMY COMPETITION STATISTICS FISCAL YEAR 1981–85

[Dollars in millions, actions in thousands]

	Army		AMC	
	Actions	Dollars	Actions	Dollars
1981				
Total awarded [1]		18,350		13,730
Competitive		7,157		3,859
Followon		2,702		2,509
Subtotal		9,859		6,368
Other noncompetitive catalog		8,491		7,362
Not considered		2,048		411
1982				
Total awarded [1]		22,716		17,437

AMC AND ARMY COMPETITION STATISTICS FISCAL YEAR 1981-85—Continued

[Dollars in millions, actions in thousands]

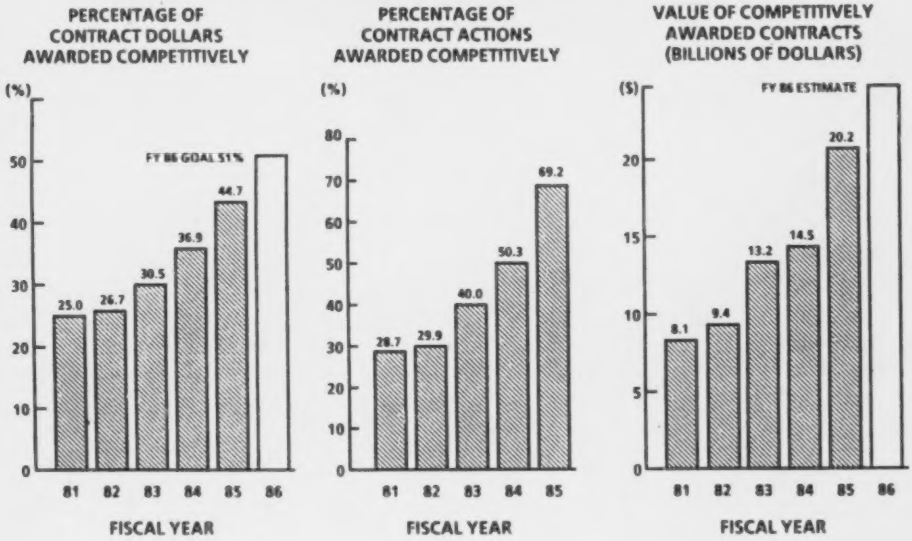
	Army		AMC	
	Actions	Dollars	Actions	Dollars
Competitive		9,160		5,336
Followon		2,443		2,279
Subtotal		11,603		7,615
Other noncompetitive catalog		11,113		9,822
Not considered		2,270		444
1983				
Total awarded [1]		24,718	454	18,862
Competitive		10,267	218	5,932
Followon		2,658	1	2,527
Subtotal		12,925	219	8,459
Other noncompetitive catalog		11,793	235	10,403
Not considered		2,519	37	407
1984				
Total awarded [1]	3,025	27,849	419	21,048
Competitive	1,725	11,781	220	6,385
Followon	3	5,938	2	5,711
Subtotal	1,728	17,719	222	12,096
Other noncompetitive catalog	1,297	10,130	197	8,952
Not considered	1,160	2,917	40	558
1985				
Total awarded [1]	2,665	31,739	383	23,599
Competitive	1,646	14,915	209	8,070
Followon	2	6,529	2	6,366
Subtotal	1,648	21,444	211	14,436
Other noncompetitive catalog	1,017	10,295	172	9,153
Not considered	1,453	3,114	73	579

[1] Statistics exclude FMS, intergovernmental and not considered for competition.

Note: Statistics on contract actions were not collected prior to fiscal year 1983 for AMC and fiscal year 1984 for the Army.

Admiral HUGHES. Procurement competition performance for the Navy is as follows:

DEPARTMENT OF THE NAVY PROCUREMENT COMPETITION PERFORMANCE



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General **Skantze**. See the attached chart on Air Force Systems Command Competitive Obligations and Actions.

AIR FORCE SYSTEMS COMMAND COMPETITIVE OBLIGATIONS AND ACTIONS

	Fiscal year 1981		Fiscal year 1982		Fiscal year 1983		Fiscal year 1984		Fiscal year 1985	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
Obligations: [1]										
Competition [2]	$3.7B	31.4	$4.4B	31.2	$5.9B	28.1	$6.2B	26.1	$10.2B	35.7
Followon	6.9B	59.4	8.5B	60.5	13.8B	65.2	15.0B	62.4	16.5B	57.7
Sole source	1.1B	9.2	1.2B	8.3	1.4B	6.7	2.7B	11.5	1.9B	6.6
Total	11.7B		14.1B		21.1B		23.9B		28.6B	
Actions:										
Competition [2]	169,932	82.9	163,496	76.4	193,544	80.0	200,027	81.2	199,645	83.0
Followon	2,516	1.2	2,496	1.2	2,354	1.0	2,223	.9	2,256	.9
Sole source	32,469	15.9	47,976	22.4	45,842	19.0	44,235	17.9	38,720	16.1
Total	204,917		213,968		241,740		246,485		240,621	

[1] The percentages for the obligations were derived by numbers rounded to the nearest thousand.

[2] Includes catalog and market price.

Source: DD 350.

General **O'Loughlin**. The following data is provided (numbers are not adjusted for inflation or a base year):

AFLC

	Fiscal year—				
	1981	1982	1983	1984	1985
Percent of competitive awards	25.2	24.1	24.4	24.6	33.7
Dollar amount of competitive awards (thousands)	2,042,971	2,246,120	2,371,385	2,844,837	3,907,812
Percent of small purchase competitive awards	55.8	55.7	[1] 65.7	[1] 72.8	[1] 74.7
Dollar amount of small purchase competitive awards (thousands)	148,746	159,353	[1] 194,962	[1] 196,246	[1] 224,118

[1] Small purchase threshold raised to $25,000, up from $10,000.

General **Babers**. For DLA, the percentage of actions and dollars competitive over the last 5 years in a constant measurement base is as follows:

	Fiscal year—				
	1981	1982	1983	1984	1985
Dollars	69.5	81.6	80.1	90.2	90.4
Actions	62.0	61.8	54.7	66.6	73.2

Senator **Levin**. One question of General O'Loughlin. You gave an example on the bid package. You said 500 bid packages were sent out at a cost of $10 to $15 each.

Senator Dixon immediately said why don't you charge for them. I think we all would agree with that. Why don't you charge for them?

You ought to think about charging them $10 or $5 for a bid package. Your point was out of the 500 you sent out, there were only two bidders.

Assume the 500 cost $10 each. It cost $5,000 in bid packages. You may have picked one other extra bidder on that contract because of the bid package. I do not know the size of the contract.

Do you know the size of the contract?

General O'LOUGHLIN. It was not very much.

Senator LEVIN. In that case, I want to finish my sentence.

But it is possible, I would think, that you could invest $5,000 to get one additional bidder and more than gain $5,000 in the price. So, I am not too impressed, frankly, by your saying, even though it sounds absurd, you only have two bidders in 500.

It is very possible even in that case that we more than made up the cost.

General O'LOUGHLIN. You and I both know anything is possible, but in a good business sense, it doesn't make that much sense to put out that many bid packages if just for a full and open competition.

If we know we have bidders out there and we know who the qualified are, we ought to limit ourselves to the number.

Senator LEVIN. My time is up. Again, I do not think I would automatically agree with you, even in that particular case, that we lost. It depends on the size of the contract and what that additional bidder brought to you in terms of reducing the price that otherwise would not be there.

I was, frankly, glad to hear from each of you that fundamentally you think that we have helped more than we have hurt this process in our reform. That is a very different flavor than we got from your boss, Admiral, in the Washington Post in July when he said that the Congress is just creating total anarchy in the procurement process. It is anarchy up there, it is by no means the Congress that he is referring to in carrying out its constitutional responsibilities.

That is a quote, not necessarily accurate, hopefully accurate, of what John Lehman said.

I am glad to hear while we make mistakes, we also do some good.

Admiral HUGHES. Our addresses referred to the procurement process. I think what Mr. Lehman was referring to is the overpublicizing of anomalies within the process. You know, one claw hammer, two diodes, for example, that we have been writing tons and tons about. That just swamps us to no avail.

Senator QUAYLE. Senator Bingaman?

Senator BINGAMAN. Thank you very much, Mr. Chairman.

Let me pick up on this issue of personnel management again, if I could.

Admiral, you had a suggestion that we take the China Lake experiment, for example, and try to broaden that. I think that is a suggestion which was essentially incorporated into what the Packard Federal Laboratory Review Panel a couple years ago came up with when it issued a report on the national laboratories throughout the Federal Government. Several of us introduced a bill, called the Federal Science and Technology Revitalization Act of 1985, in response to the Packard Panel's report.

This is a bill that we introduced early this month, Senate bill 1727. Senator Quayle is cosponsor as is Senator Goldwater.

I would be interested in getting any reaction that any of you have to that.

What it tries to do is allow more flexibility in the personnel management system, particularly for scientists and engineers, and really tries to take the kind of experience they have had there at China Lake and a few other places, I guess the Naval Ocean System Command in San Diego as well, and has tried to say, OK, at least for scientists and engineers let us go ahead and have a more flexible system.

Possibly we need to cover not only scientists and engineers, many of whom are in the procurement end of things, but also cover more generally people involved in acquisition and this kind of thing.

I would be interested in anybody's reaction.

General THOMPSON. We in the Army support this legislation. It allows us flexibility in the overall administration. It also allows us to make sure that performance is the key and we think that is a very, very real incentive for us and for the people involved.

We do have problems getting quality scientists and engineers. We might suggest that we also look at the procurement community in this regard because I think there are similar applications there to be considered.

Senator BINGAMAN. You think it possibly should be broadened to cover more people involved in procurement than just scientists and engineers?

General THOMPSON. Yes, sir. We think our procurement people, from the Army's standpoint, ought to be treated as professionals and carried in a professional career field as are scientists and engineers.

Senator BINGAMAN. General Skantze, you say in your testimony, you recommend that Congress direct OPM to establish at a minimum a system contracting specialty as a professional series.

General SKANTZE. Yes.

Senator BINGAMAN. I gather that is along the same line we are talking about?

General SKANTZE. That is correct. I think certainly your legislation has merit and I think would be useful in providing more flexibility, but in all candor, in my judgment, our major problem is in the procurement career field.

At least from my standpoint that we are holding our own on scientists and engineers, at least at the moment. The more difficult problem is the procurement career field because those people are as important to the procurement acquisition process as the scientists and engineers. You cannot do without either one.

So, to make them a professional career field would enormously enhance our ability to get better people.

Senator BINGAMAN. I will not go into detail on it, but we have quite a few statistics indicating we were not holding our own with regard to scientists and engineers as far as being able to hold on to good people and attract them.

I do not dispute your point about the need for more professionalism in systems acqusition.

General SKANTZE. In general, looking at both people in uniform and our civilians, we are holding our own. We go through the attrition process where the exacerbations are in the high competitive cost areas I mentioned.

To compete in Los Angeles for procurement people or scientists or engineers in the civilian work force is an extremely difficult process.

Senator **Bingaman**. One figure that we cited was that in 1984 a GAO report indicated Federal agencies employing engineers experienced a disparity of 47 percent at the experienced GS-11 level.

So, I think there is some kind of problem there.

Admiral, did you have any comment on the legislation or the broadness with which we should approach the problem?

Admiral **Hughes**. One of the criticisms that I pointed out is that it costs us a total of 5.6 percent more dollars for the employment of those people over a 4- or 5-year period. We think we can bring it down to less than 1 percent a year in the case of the engineers and I think the same thing would happen if you included acquisition personnel.

It would probably cost you a few more dollars as a bottom line, but, of course, what you are buying for it, in my mind, is very worthwhile.

Senator **Bingaman**. General Babers, you said that you felt there was a need to address the professionalism of the personnel.

I gather all of you are saying that in spite of the fact maybe we have done more than enough legislating on some of these procurement requirements, that the need for addressing the professionalism of the personnel is an exception to that and that is something you think is appropriate for Congress to get into.

General, did you have any thoughts as to whether this is the right direction to go?

General **Babers**. I think it is the right direction to go. Ultimately, every problem I have checked out in the last 3 years associated with procurement has had its inception someplace down about the GS-7 or GS-9 level. Somebody doing his best, who did not understand what was going on, or who had so much work on the table, did not pay sufficient attention to something; or someone in the supervisory chain did not fully comprehend all the issues within his responsibility that were surfacing in a given day.

Senator **Bingaman**. General O'Loughlin, do you have any comment?

General **O'Loughlin**. No; other than we support S. 1727. It would help us in one of the side effects of breakout. When we break out parts to subvendors, we lost the engineering talent from the prime. He handles a considerable number of engineers that certify and make sure that the subvendor is in good shape. We have had to pick that up.

As a result, we have had to go out and hire engineers for source qualification and to make breakout decisions. In competing mainly, just competing in the competitive market for engineers has caused some problems due to the wage disparity, what we can offer versus what they can get out commercially.

Senator **Bingaman**. Let me ask one other line of questioning here.

Senator Nunn has suggested that because we have all the regulations and laws overlaying the acquisition system today, that maybe it is worthwhile trying a pilot program on a few weapon systems which would move away from this current trend and essentially waive a lot of these regulations, and see how that would work in particular systems.

I would be interested in knowing if that is something that you folks would support; if so, how would we go about choosing which systems to include in such a pilot program?

Is there a workable way to assess or test the need for all this that we have put on in the way of laws and regulations?

General **Skantze**. I think the major concern to anybody who has ever run a program, and I have run several, is program stability.

If you could give direction and funding and approve the technical content and schedules and tell that individual who is going to manage that program to proceed and use his best business practices, many of which currently exist in existing statutes and regulations, all of those things do not necessarily hamper, but we could run an optimal program and get out of the micromanagement aspect using existing statutes and regulations, many of which on their own are logical business ways to go about it.

I think with that kind of stability you could have great success with pilot programs of that nature.

Senator **Bingaman**. You think it would make sense for us to essentially permit the waiving of the statute or regulatory constraints we have imposed with regard to certain specified programs that the services or the Secretary of Defense would identify?

General **Skantze**. Only those that are inhibiting because a lot of them are good commonsense business practices which we follow anyway.

General **Thompson**. I would like to see such a program if we are allowed to make recommendations as to what programs should or should not be included. In some areas we have to get our own house in order. Areas like settling on our own requirements and staying with those requirements, getting away from the heel-to-toe kind of philosophy and making sure that the entire chain understands what it is we are trying to do and accepts those kinds of changes.

I would like to see this kind of program and I think it would pay some real benefits.

Senator **Bingaman**. Thank you. That is all I have.

Senator **Quayle**. Senator Dixon?

Senator **Dixon**. General Skantze and General Babers, you both have testified, and I have no quarrel with your position, that salaries are too low in the procurement and acquisition field.

I believe, General Babers, you said there was a 16-percent attrition in that area as a consequence of that problem. There are two points I want to make here.

The Preparedness Subcommittee dealt with this very problem. The Commander-in-Chief asked for a 5-percent salary cut on the civilian side. We made a restoration of all those funds and protected the freeze, which is not too good, but better than the 5-percent cut.

I wonder if the feelings of all the four-star people in the room today ought not to be conveyed to the Secretary of Defense and Commander-in-Chief and others since it is quite apparent that you view this salary problem as a serious one.

General BABERS. Sir, I think it would be misleading to attribute the attrition problem solely to the salary level. That plays a role, but it is not the total problem.

We need to look at, among other things, the total professional opportunity for growth, for promotion, and for schooling, which play a role in the attrition problem. Salary plays a role, but it is not the total role.

Senator DIXON. Incidentally, in that connection, may I say, General Skantze, that I am informed that the Air Force is downgrading contracting officers around the country from GS-11's to GS-9's.

I wonder how that squares with the testimony here today about your concerns. I know it to be a fact that at Scott Air Force Base all contracting officers are on notice as being downgraded from GS-11 to GS-9.

May I have a comment on that?

General SKANTZE. If it is Scott Air Force Base, they are not in the acquisition business. I suspect that is the base procurement people. There is a difference between people who do base procurement and buy the local kind of things and the people we are talking about who manage and negotiate multimillion dollars worth of contracts.

Senator DIXON. You would not suggest that there is less important work being done at the local level in acquisition?

General SKANTZE. There is a difference in the kind of work that is done. The base procurement level deals with what I would call the steady stream of buying housekeeping items on a regular basis. It is a more routine operation than dealing with the full acquisition process and putting out purchase orders and buying and negotiating quantities of spare parts and different high-tech items.

General O'LOUGHLIN. I think that is part of a larger problem, that is, grade creep. We have fought that in Logistics Command and it is not occurring at all.

We have made some adjustments to the number of people that we put into competition advocacy and in other procurement areas by increasing authorized and by moving grades to insure the right structure.

I think it is symptomatic to what Senator Quayle mentioned as far as the civil service personnel program you must be able to hire the people you need to insure the right system structure. We are constantly taking hits for grade escalation and pressured to keep the grades down.

That may have been Scott's way of doing it. In our command we did not reduce anybody.

Senator DIXON. Let me say I note in the testimony which I am pleased with that your competition percentages are increasing in the Air Force from 26 to 36 percent.

Was that the testimony, General?

General SKANTZE. Yes.

Senator DIXON. In the Army, from 31 to 34 percent.

General THOMPSON. Yes; for the Army Materiel Command.

Senator DIXON. I do not recall the Navy figures. Admiral, do you have those?

Admiral HUGHES. They are about 26.7 to 44 percent, 1982 to 1985.

Senator **Dixon**. I guess, Mr. Chairman, I would be compelled to observe the reverse of that would be, for instance, in the Army we still do not compete 64 percent or 66 percent, in the Air Force, 64 percent by municipal or State standard that, of course, would not be considered a very good record.

I would say that we ought to continue to seek more competition in our efforts in all the branches of the service.

General **Skantze**. May I make a comment, Senator?

We have a category called follow-on competition. The F-16 was competed, the B-1B was literally competed against the ATB. If I could count that $8 billion I put on contract for the B-1B's in 1985, I would go from 36 to 50 percent.

The more important figure is how much sole-source contacting do we do in terms of dollars. I suspect among all of us it is less than 10 percent.

Senator **Dixon**. If you have some breakdowns on that, I would very much appreciate having that.

General **Skantze**. We can provide it.

[The information follows:]

General **Skantze**. The information on Air Force Systems Command Sole Source Obligations is provided on the attached chart.

AIR FORCE SYSTEMS COMMAND SOLE SOURCE OBLIGATIONS

[Percent of total business]

	Fiscal year—				
	1981	1982	1983	1984	1985
Sole source	$1.1B	$1.2B	$1.4B	$2.7B	$1.9B
Percent	9.2	8.3	6.7	11.5	6.6

General **Loughlin**. The following data is provided (numbers are not adjusted for inflation or a base year):

AFLC

	Fiscal year—				
	1981	1982	1983	1984	1985
Percentage of sole source awards[1]	74.7	75.9	75.6	75.4	66.3
Dollar amount of sole source awards (thousands)	6,054,544	7,067,981	7,360,922	8,705,256	7,702,863
Percentage of followon awards	45.6	45.3	31.9	52.6	43.4
Dollar amount of followon awards (thousands)	3,692,183	4,217,590	3,105,444	4,915,774	5,043,393
Sole source—excluding followon—true sole source:					
Percent	29.1	30.6	43.7	32.8	22.9
Dollars (thousands)	2,362,361	2,850,391	4,255,478	3,789,482	2,659,470

[1] Sole source is defined as a noncompetitive procurement, or: followon after price, design, technical, or other competition; other noncompetitive; or catalog or market price. This terminology is based upon DD350 coding.

Senator **Dixon**. General, you made a statement about the Freedom of Information Act. I think you said that more than 14 man-years were involved in complying with that act from a standpoint of procurement and acquisition. I may be slightly misquoting you. Could you correct me if I am wrong about that?

General **Skantze**. I said 14½ man-years and $515,000.

Senator **Dixon**. Each year are spent in complying with the Freedom of Information Act, or last year?

General **Skantze**. The 14 man-years are an aggregate. If you put twice as many men on it, you do it in a half a year; four times as many, you do it in a quarter. In aggregate, the number of people, hours working on sifting through records and synopsizing.

Senator **Dixon**. Do you mean to say in a year that was the amount of time expended on that purpose, over half a million and 14½ man-years?

General **Skantze**. Yes.

Senator **Dixon**. I was interested in that because while I believe the Freedom of Information Act ought to let the media and others know what is happening, I suspect what you are saying is that a lot of these requests are people seeking a commercial or other advantage in making these inquiries.

I would want the subcommittee to note that I do not think anybody on the subcommittee would want in any way to impair the right of the media representing the public at large to know what is taking place.

I suspect I would speak for the subcommittee in saying this, that I do not know any reason why we ought to be spending that kind of money and man-hours helping commercial vendors to get information that may give them a commercial advantage they otherwise would not have.

I think your point might be a very good one.

Admiral **Hughes**. I would like to expand on the Navy's experience. I find this gross, myself. We have almost third-party people involved in the Freedom of Information Act now.

We have pretty good evidence and suspicion that there are little companies set up to drain the hell out of us and sell what they get. We have a 10 man-year backlog in our Air Systems Command alone where they have requested every training manual and over 100,000 drawings of the P-3.

Senator **Dixon**. I am very concerned. I would like to have that information. I know all five of you recognize the very delicate nature of this area of inquiry because the people's right to know in a great democracy like ours is obviously paramount. I would not want to do anything to limit the people's right to know.

[The information follows:]

General **Skantze**. While we process a number of requests from researchers, news media, historians, students, writers, and curious individuals, the majority of our Freedom of Information Act requests come from business firms who are collecting information on their competitors. During the first 8 months of 1985, we processed 103 denials; 52 of these involved proprietary business or trade secret materials. (See the attached chart for AFSC Freedom of Information Activity Jan–Aug 1985.)

While there is an exemption to protect proprietary data, invoking that exemption is extremely expensive. The courts have mandated that we conduct a line-by-line review of full contracts/proposals to determine if there are portions which can be released. Individuals who conduct these line-by-line reviews must be experts in contracting, experts in FOIA, experts in law, and experts in market conditions. Normally, FOIA reviews are conducted by our contracting staff who must squeeze these "additional duties" into an already busy schedule. Due to the enormity of these contracting files, these "additional duties" take on stupendous proportions. A single FOIA request for proprietary data may take weeks to examine.

The figures presented in the chart are not all-inclusive. They do not include the many manhour costs which go unreported: those involved in the legal review process; clerical costs to type intra-agency memos: costs to handcarry FOIA requests;

costs to conduct the pre-disclosure notification; telephone costs; costs to consult with experts. The expenses which actually get reported are a fraction of the true costs involved.

The Act itself calls for the recoupment of direct search and reproduction cost only. Reported search costs for the 8-month period totaled $8,030. We recouped 58% of these. we xeroxed $16,015 worth of documents but were reimbursed only $11,667 or 73%.

The average cost to AFSC to process a single FOIA request starts at $114. Of this, requesters pay about $5.75. FOIA provides a low cost means to gain access to commercial data normally not available and an extremely low cost method to have that data reproduced. Business firms are avoiding reverse engineering costs (i.e., costs of purchasing a piece of equipment and dismantling it to examine engineering features) as well as costs to hire individuals to "spy" on their competitors. One firm periodically requests, under FOIA, the HQ AFSC inspection schedule for contractors for the stated purpose of contacting them prior to the inspection to market their pre-inspection services. Another agency received a report from a firm followed immediately by a FOIA request for multiple copies of that same report thus appearing to avoid reproduction costs. Providing business firms with such bargains at the expense of the submitter and the U.S. Government was certainly not a result contemplated by Congress when FOIA was enacted.

As a result of the above discussion, we recommend that the FOIA be amended:

a. To protect the Government's valuable property (technical data, manuals, etc.) from release under FOIA by redefining "record" to exclude Government resources;

b. To exempt from release in their entirety procurement records containing competitive sensitive and advisory or deliberative information;

c. To exempt from release commercial data in its entirety;

d. To extend the time in which the Government must respond to requesters.

AFSC commandwide freedom of information activity—January to August 1985

Requests received	2,835
Requests denied	103
Denials involving commercial data	52
Costs:	
Salaries, FOIA staff	[1] $227,239
Salaries, other	[1] 46,250
Reproduction/computer costs	[2] 16,557
Postage, electromail, etc.	[3] 19,997
Routine release costs	[4] 11,811
Total	321,854
Man-years:	
FOIA personnel	11.473
Other personnel	2.200
Total	13.673
Fees collected:	
Search	$4,646
Reproduction	11,667
Total	16,313

[1] Salaries are priced at $8 per house clerical time; $16 per hour professional time; and $26 per hour executive time. These rates are established in DOD 5400.7-R.

[2] Reproduction costs are priced as follows: Preprinted material—1¢ per page; office reproduction—10¢ per page; microfiche—25¢ per print. Computer costs are priced at the actual cost to operate the central processing unit. These rates are established in DOD 5400.7-R.

[3] This figure includes $6,168 for training costs.

[4] This cost covers personnel costs to release regulations and other routine documents to the public.

Admiral HUGHES. The attached paper is provided in response to the question.

Navirtechservfac FOIA Impacts

SYNOPSIS

The recent Department of Justice opinion to place NAVAIR technical data (engineering drawings and technical manuals) within the meaning of the term "record" under the FOIA creates adverse impacts relative to control and release of technical data, dual processing procedures, NAVAIR pricing and recovery costs and present personnel resources. Non resolution of these impacts will result in degradation of NATSF's primary mission in support of fleet requirements and precludes adequate export control of technical data technology transfer to U.S. Adversaries.

IMPACTS

A. Prior to DOJ opinion, all requests for technical data were processed as Non FOIA exemptions under SECNAVINST 5720.42C. Requestors for technical data who establish a legitimate business interest were provided the technical data as Non FOIA Cash Sales. Such action reasonably assures that Military technical data was not automatically released to the general public, which can be considered tantamount to foreign disclosure. Under the present DOJ position, technical data under FOIA provides little or no protection from releasing commercially exploitable data to the public, and provides a potential path for military technology transfer to U.S. Adversaries.

B. Under the DOJ's opinion, NAVAIR is now faced with the arduous administrative burden of processing technical data requests under two separate procedures with dual pricing methods as follows:

Category	FOIA	Non-FOIA
Direct search (per hour)	$8.00	$9.60
Duplication:		
Manuals (per page)	.01	.03
Aperture card dwgs (per card)	.03	.60

Technical data provided is identical except for the type category. Therefore, the probability of the private sector legal pricing appeals appears imminent in favor of FOIA.

C. NAVAIR does not recover costs under FOIA since payments are made directly to the U.S. Treasury. Further, FOIA costs exclude all indirect labor charges, all equipment operating/maintenance costs, all special supplies and chemicals, and exclude Foreign Military Sales developmental costs. Naval activity operating funds will be used to totally subsidize public sector FOIA requests.

D. Under the current DOD Directive 5230.25, a clear definition of critical technology concerning NAVAIR's weapons, systems, and equipment does not presently exist. Therefore, the hulls of incoming technical data requests will be controlled under FOIA. Current backlog of private sector requests for engineering drawings is approximately 4.6 million frames, which equates to a 10 manyear effort. Placing the entire backlog under FOIA will have a serious impact on our present resources primarilly dedicated to fleet support and BOSS/Breakout initiatives.

E. Recent court decision, to provide Newport Aeronautical Sales Company (NAS) NAVAIR technical data under FOIA procedures, has resulted in releasing over 35,000 technical manuals to a data broker. In addition, NAVAIR was further directed by DOJ to provide duplicate requests to said data broker. NAS now possesses over 90% of all NAVAIR Technical Manual and their customer listings reflect U.S. and foreign government activities. Under the court order of April 1984, to data, unreasonably processing time frames have been imposed upon NAVAIR's repository and has resulted in diversion of personnel from mission tasks causing various backlogs to develop. The NAS court decision has established a precedent and two additional companies, represented by the same counsel have been successful in their appeals directing release of processing of technical data under FOIA by General Counsel. One request submitted by Pacific Sky Supply requires approximately 100,000 drawings for the P3C aircraft. The second company Electro Methods Incorporated (EMI) has in excess of 2,000 engineering drawing part numbers. Since these requests are under FOIA appeals, prompt processing is being requested by counsel to preclude possible court litigation. Such actions under FOIA preclude processing technical data requests in the order of receipt and causes extreme administrative burden in responding to numerous counsel letters and appeals.

General O'Loughlin. We cannot provide precise statistics on those Freedom of Information requests which are used by vendors to attempt to gain a commercial advantage. However, the following data will provide the scope of activity with which Air Force Logistics Command is involved with Freedom of Information Act requests:

	1984	[1] 1985
Estimated total cost (thousands)	$532.7	$424.3
Total amount collected (thousands)	$29.1	$17.4
Net estimated cost (thousands)	$503.6	$406.9
Estimated total man-years used	16.8	12.1
Total reported requests	6,405	4,081
Total denials (including partials)	973	755
Denial rate (percent)	15.2	18.5
Number of instances of participation by commander, vice commander, Chief of Staff	87	316

[1] Through August.

General Thompson. Our experience has been that very few of the requests for information received under the auspices of the Freedom of Information Act (FOIA) are generated by the media. During FY 1985, of the 189 FOIA requests processed through the HQs alone, only 12 were requested by the media. Several were originated by organizations, such as Common Cause, American Friends, Federation of American Scientists, but the remainder were originated by commercial firms or individuals. We conclude that in most these latter cases the parties are seeking information that may help in litigation against the Government or assist them in competing with other firms to obtain Government contracts.

For example, a recent FOIA request was received from a law firm asking for "copies of any and all studies, reports, surveys, investigations, plans, contracts, memorandum and correspondence for the period beginning 1 Jan 80, to the present, concerning or relating to "a certain company. The requester is not required to specify the purpose of his request, however, such a request can only be interpreted as an attempt to gain information on a specific firm including information which could be competition sensitive and of great value to other firms. These type requests can severely interrupt an agency's mission accomplishment when current work must cease until the requested documents are located, reviewed, releasability issues decided, copied and dispatched to the requester. For example, an existing request, onogoing since June 1984, has consumed thousands of manhours throughout the Army with 20,103 pages of documents already provided to the requester.

General Babers. The Defense Logistics Agency shares the concerns expressed on the availability of technical data under the Freedom of Information Act (FOIA). We have long held the view that formulae, designs, drawings, research data, computer programs, technical data packages, and similar assets are commercially exploitable resources which should not be released to the general public under FOIA, and in that respect is similar to other types of property. The principal value of this data is commercial. It contributes little, if anything, to public understanding of Government programs, operations, and activities. We do not believe Congress ever intended the use of FOIA as a vehicle for private economic activity or for the transfer of these resources to the private sector; but that is the situation we face today.

The Department of Justice (DOJ) believes that we should treat technical data as fully within the purview of the FOIA, forego any general claim of exclusion, and rely upon Section 1217 of the Department of Defense Authorization Act, 1984 and other available exemptions under FOIA to protect technologies sensitive to national security, the proprietary rights of our contractors, and other interests. The DOJ view flows from interpretation on what constitutes "record" under the FOIA, and does not address the issue as a matter of public policy.

We do not see a general exclusion for technical data as inconsistent with the interests of an informed citizenry. We are not dealing with the media, public interest groups, or concerned citizens in this area. We are dealing with business entities whose sole ostensible purpose is to acquire the data for its commercial value—and we are doing so at considerable taxpayer expense. We recently spent $300,000 on a single request in segregating releasable and unreleasable technical data.

The use of FOIA for private economic interests is broadly inconsistent with the objectives of the Act. We believe a general exclusion from its provisions for technical data would eliminate the abuses without diminishing the interests of an informed citizenry.

Senator DIXON. My opinion is it is being used for a lot of other purposes. That it has nothing at all to do with letting the public know about the operations of this Government of ours.

Admiral HUGHES. We were okay until fairly recently when the Justice Department implementation changed the definition of records. It began to include things that we previously had not, by our own definition in defense, included as records; for instance, business information.

Senator DIXON. Crucial technical data?

Admiral HUGHES. Yes. We had excluded that in our own Department of Defense definition, but that has since been set aside by the courts and the Justice Department has directed us to change the definition. In doing that, the door is open.

Senator DIXON. I would like to have that information and evaluate that. I do not want you to go into a lot of trouble to prepare a lot of public documents, but——

Admiral HUGHES. A 2-page point paper is available.

Senator DIXON. To the extent you can evaluate that for us, we would appreciate it because it is a significant point.

I want to say in conclusion, that as the main sponsor of the Competition in Contracting Act and one who was involved in the two major jurisdictional committees, Small Business and Armed Services, and I do not mean this offensively, but I get from your testimony that while you generally approve of the procurement legislation, most of you do not like very much those sections which particularly helped the small businesses, such as the certificates of competency, requirements, and information on how a vendor can qualify, and breakout procurement center people employed by the Small Business Administration.

While I do not want to engage in a quarrel with you, I want to say those are areas that we spent much time on in arriving at our decisions about the legislation and I would want to second what Senator Levin said when you talk about changing the threshold.

For example, it is not quite as simple as just saying we are going to change the threshold a little. Those things did occupy a great deal of time in both committees, and I would suggest that we have some commitment of considerable work effort involved in that legislation.

But we appreciate very much your honesty in giving us your evaluation of the legislation.

I thank all five of you for sharing your opinions with this committee.

Senator QUAYLE. Senator Glenn?

Senator GLENN. Thank you very much, Mr. Chairman.

I apologize that I could not be here earlier, I had other commitments this morning.

I want to thank you, each of you, for the support you gave last summer when I had the DOD procurement conference across Ohio. General Babers, DLA, sent mobile displays which were very good. I want to do some more of that in the future. I appreciate the support you gave in that area.

When Secretary Wade was here before, we talked at some length with him about acquisition, technical data rights, and who gets it and putting it out to second sources. I want to get into that area, but I am afraid about going too far. It is a very sticky area.

As I interpret the statute, it requires both fairness and balance and that is easy to say, in data rights, and to make available to DOD technical data to enhance competition for replenishment of spares procurement and other things, at the same time protecting the legitimate rights of industry to its privately developed technology.

The contention of many in industry is that the proposed implementing regulations do not reasonably balance the interests of the Government and that of industry, but really favor the Government.

I am concerned about another area and that is when we do this, when we do such things as General O'Loughlin talked about here, how the Air Force is handling proprietary data and reverse engineering and things like that, we really discourage, it seems to me, some of the private research and development that we are trying to encourage.

We are just getting into this in the Star Wars, SDI, business in which we are going to have thousands and thousands of contractors doing very, very technically oriented research work. A lot of it will be on a straight Government contract, there is no doubt on that, on a straight Government contract, with a company that is set up solely to deal in that area.

There is no doubt in my mind about proprietary rights to the Government. When you have large companies, and many companies dealing in Star Wars are large companies, they have research funds. What is proprietary and what is comingled funds with the Government, and so on, gets to be very sticky.

I do not have the answer to this. I would like some guidance from you gentlemen as to how we take care of this. It fits into a bigger picture, too. The Soviets can outnumber us in almost every weapon system, I have no doubt about that. But we can outdo them in this high tech area. We can be better. We can provide more fire power for each person through our technical capability.

We do not want to cut back on research and cut back on the inventive, inquisitive way of Americans doing this in our industry that gives us these new weapons systems. There is a balance to be hit and I have no idea what it is. I would appreciate your comments on this.

General, in reading your testimony here, even going into reverse engineering, if the contractor will not release data to you when you request it, you put a team of engineers on it on reverse engineering and get it anyway.

If I was doing R&D, you might catch me once, but you would not catch me twice. The next time I try to put some money in research it may not hit, so I may have four dry holes for every time I hit with something good.

But every time I hit something good you will reverse engineer and outdo me. How are you going to take care of that? How are we going to encourage research and at the same time make sure we have the data rights to encourage competition and yet not be unfair?

General O'LOUGHLIN. I do not think that all your fears are warranted, sir, because I think what we have done with our rather meager reverse engineering program, it is $5 million which is not meager; to the business I am in, it is. We limit usage of reverse engineering only to items that have taken quantum jumps in price since the last purchase.

I deal primarily in parts for aircraft that are up to 25 years old. First of all, price dictates whether we take a look at it. We look at the item and if there has been a quantum jump in price, we consider reverse engineering. For example, we recently had a KC-135 constant speed driveshaft jump in price from $180 to over $600.

We thought that was not a fair and reasonable price. We asked the vendor for the data. He said no, I am not going to give it to you. So, we went with our engineers, who used CAD/CAM to reverse engineer the item. We estimate that we can produce the item for around $100.

That is when we make decisions to reverse engineering. We are not saying, we are going to steal your data. The thing that normally dictates whether I reverse engineer or not is available supply of the vendor, whether he really wants to tool up on a 20-year-old item or whether we can afford a work stoppage in a depot on a part that is 2 years away from being delivered.

That is the extent of our reverse engineering at this time.

Senator GLENN. Do you have any certain length of time you would not reverse engineer anything, less than 10 years old, or something like that, or do you do it on a case-by-case basis?

General O'LOUGHLIN. We do it on a case-by-case basis in a very limited manner. In regard to proprietary data, the ones I hear from the most, to be honest, is the small guy, a small vendor who has developed a commercial proprietary design, and who, if he were to give it up in the competitive world and allow everybody else to have that data, would lose his edge in the competitive market. This is very troublesome to the small business guy whose livelihood is dependent on this crown jewel, this data which makes him competitive in the commercial world.

That is the complaint I hear most. "Why do you make me give up that proprietary data?"

Of course, we have policies that say if you want to compete, you had better be willing to give it up.

Senator GLENN. You run up against this.

Does anyone else have any comment?

General SKANTZE. Yes. I have found that on a large-scale acquisition that the primes generally are going along with the policy. I have the waiver authority for the subcontractors and vendors.

On a case-by-case basis when a prime comes in and says I cannot offer you Harry Smith's data for the piece we are building for you, we take that on a case-by-case basis and we will issue waivers as we think it appropriate to protect the kind of process that General O'Loughlin has mentioned to you.

We have recently constituted a data rights groups for the JLC who is going to look at the issue in totality because a lot of us deal with the same complaints. We do not want to be inconsistent with how we approach the problem.

We take very serious concern as you do, and as a group, we are trying to address it on a very objective basis.

Senator **GLENN**. I know you gentlemen are trying to do the job in encouraging competition out there. However I am concerned that we do not discourage people who are putting their own research bucks out and are not hitting. We want to make sure we get as fair an exchange on competition as we possibly can.

I am concerned that we keep research going as much as possible. In private industry we have tried to give incentives, and so on. President Reagan said, "If basic research is worth doing, private industry will do it." That was the basis on which the administration cut back 29 percent on basic research, that it was sure industry would do.

Even cutting back on basic research in the first year of the administration I thought was a very foolish thing to do, especially when we are coming into more research competition around the world, but it was done.

The idea was that industry would do it if it was worth doing. But I think there are some research areas that are so highly speculative that they fall in the province of Government, and we should be taking up that area. I also want to get as much research money from industry as we possibly can in these areas.

If you have any thoughts, I would appreciate your putting them on paper and sending them to us so that we can include them in the subcommittee record.

[The information follows:]

General **THOMPSON**. We agree that in our efforts to obtain competition we must not forget the need to encourage industry to invest in research. As a customer, however, our primary interest is in satisfying our requirements at the best price considering the total life cycle cost of the program. The best way to insure that follow-on prices for items, including logistics support for these items, are reasonable is through competition. That is one reason our performance is being measured on the extent of competition achieved.

We can deal fairly with industry in the area of reimbursing them for their development costs and can work with them to protect and compensate their research initiatives. This can be done through proper planning of our data needs, up-front determination of rights, early agreement as to how and when rights can be purchased and flexibility in the negotiation and selection process. Where industry is arbitrary and unreasonable in providing us rights in data, however, other measures may be necessary to insure that the Government is not placed in the position of repetitive sole source procurement at a less than advantageous price.

In todays environment of competition for budget dollars and demands to reduce the deficit, and further considering the emphasis to reduce the time for system development, the trend is moving more and more to requirements based on reduced risk and minimum need as opposed to technological advancement. Thus, while we agree that in order to enhance our technological superiority an increase in the amount of research accomplished either thru direct funding or reimbursement would be desirable, this may no longer be possible.

Admiral **HUGHES**. Finding ways to encourage private industry to invest their own funds in research aimed at developing or improving items used by DOD is a difficult and complex undertaking.

Industry investment is usually linked to probabilities of return on investment. Larger companies with conservative strategies look to the surest, greatest returns. Encouraging anyone to speculate has become increasingly difficult as the cost of developing complex defense equipment has risen. Reimbursing independent research and development costs related to defense needs is the principal means by which we encourage private research. Value engineering programs are also useful means to incentivize contractors to improve items.

General **SKANTZE**. Technical innovation is essential in order to maintain, over potential adversaries, the qualitative edge in military systems. Private sector investment in basic and applied research complements the Government's technology base funding levels. We have been successful in encouraging this private investment through a cooperative program called Independent Research and Development (IR&D). The IR&D program is a strategic, long-range R&D program chosen and conducted by the contractor to maintain and improve technical competence and competitive position.

The DOD recognizes IR&D costs as a necessary cost of doing business. Currently, the DOD pays only forty cents of each dollar of IR&D expenditures, but has limited rights to the results of the total program. One major advantage to industry is the ability to market technology with full data rights belonging to the contractor and not the Government. Unfortunately, IR&D is seen as a prime target in efforts to reduce the DOD budget. Congressional hearings in 1983 resulted in a maximum limit on total IR&D ceiling dollars. Any further reduction in IR&D ceilings would be counterproductive.

With less IR&D dollars available, industry will focus their IR&D program on efforts which have a near-term payoff. Strategic long-range R&D efforts will not receive the necessary level of private investment, thereby increasing DOD R&D expenses during system development and delaying our ability to react timely to national security threats.

General O'Loughlin. AFLC has expanded its role in the Independent Research and Development arena in the last few years. This effort has been primarily through the Air Force Acquisition Logistics Center (AFALC) whose mission is to increase readiness and sustainability and decrease the life cycle cost of weapon systems and equipment. To achieve this, the AFALC has increased its attention on prime contractors' early logistics IR&D efforts. The AFALC and our other air logistics centers have:

Provided logistics evaluators in annual contractor IR&D reviews.

Identified logistics R&D needs (specific as well as generic) for potential Air Force laboratory and/or contractor IR&D activities.

These efforts are administered by the Air Force Coordinating Office for Logistics Research (AFCOLR), to which AFALC provides logistics and engineering support. These activities involve leveraging approximately $5 billion of contractor R&D activities annually.

In addition to AFALC's involvement, this year we challenged each of our top fifty defense contractors to increase their submission of value engineering change proposals. Value engineering is a technique whereby a contractor proposes an improvement to a part or process under an existing contract and, upon acceptance, shares resultant savings with the Government.

Aside from these two areas, we are not otherwise involved in encouraging industry to invest in research, and do not have specific recommendations. However, we do believe that program stability must be improved in order for industry's expectation of recoupment on its investment to be improved.

General Babers. The Defense Logistics Agency has no policy in the area of research. However, it is my belief that industry involvement can best be elicited where incentives can be made available. A good example lies in use of the Department of Defense Industrial Modernization Incentives Program. In this program, defense contractors are expected to spend their own money in modernizing their equipment and facilities to gain improvements in productivity. The specific projects for investment would have more risk than contractors would normally accept but they would have substantial payback, nevertheless. The incentive for contractors to make such investments would be the Government's willingness to share, in a meaningful way, the savings resulting from the investments or to indemnify contractors for unamortized losses that might occur subsequent to investment. The availability of this program may stimulate many contractors to develop their conceptual ideas for productivity improvements to the point of investment through research and development.

General Thompson. From Army's standpoint, we totally understand industry's position. We are in somewhat of a dilemma here. If we want to compete, how do we obtain the data necessary to compete?

We want the best technology available and we recognize industry's contribution; that is, what they have done in the area of research. We have a proposition out for public comment now to try to get people to suggest methods of improving in this area and to broaden the base of people who can help us come up with equitable ways to resolve this issue.

Senator **Glenn**. It is particularly difficult, and I make this as a closing statement, where the big companies have comingled funds. They have a Government contract and it provides for a certain level of research. If they think it looks promising, they are willing to put out company funds to help that out.

Then you get into who furnished the money for what situation. It is very difficult to sort that out. We have had several manufacturers back home in Ohio who have talked to me about this where they were concerned about it.

Goodyear had some problems where they put some money in research on brakes. You have been in the brake and wheel assembly type situation where they were being asked for certain of their technical data so that it could be completed, on something they developed with company funds.

It is a difficult area. I would appreciate any comments you might forward to the subcommittee to help us out in that regard.

[The information follows:]

General **Thompson**. Independent Research and Development (IR&D) is, by definition, "cost that is not sponsored by, or required in performance of a Government contract or grant." Consequently, there cannot legally be a comingling of IR&D with funds provided under R&D contracts.

The comingling problem is in trying to sort out which items/components under a contract were developed from private sources and which were developed at Government expense. If an item is "developed at private expense" (including IR&D) the Department of Defense gets no data rights and we are generally locked into a sole source situation unless some arrangement to purchase rights is made. The Government always has the right to challenge contractor's proprietary claims to data and there is constant conflict as to whether an item was developed under a Department of Defense funded contract or IR&D. At present, there is no clear definition of "developed" within the phrase "developed" at private expense. The DOD proposed data rights regulations which is out for comment does contain such a definition.

A suggested solution to the data rights problem would be to procure the necessary data rights as early as possible in the acquisition cycle.

Admiral **Hughes**. The problems associated with sorting out the respective rights of a contractor and the Government in situations where both parties funded aspects of the development of an item which DOD acquires are complex. Contractors can provide data with limited rights only if the items, components, or processes which the data pertain to were developed at private expense.

This requirement has been interpreted to refer to complete development. Under DOD funded development contracts, contractors can, and do, limit the Government's data rights with respect to particular components that were developed exclusively at private expense. Thus, even though DOD is paying for the development of an item, it is possible for DOD to end up with less than unlimited rights in all of the data delivered under the contract. In many instances, this fact makes it difficult or impossible for us to reprocure the item competitively. The Navy is, however, prepared to pay a fair and reasonable price to acquire rights to permit future competition when it makes sense to do so.

DATA RIGHTS

General **Skantze**. Running counter to efforts encouraging IR&D, is the Government's initiative to acquire data rights to facilitate competition. The Air Force is concerned with seeking a balance on ownership of data to ensure availability of adequate reprocurement data to compete high volume spare parts and, at the time, to protect valuable private property. In 1984, the Under Secretary of Defense for Research and Engineering completed an extensive study in this area.

The study concluded the following: data rights are not the major problem preventing DOD from obtaining competition; the Government does not need unlimited rights to all data; forcing contractors to give up unlimited rights as a condition of doing business with the Government is not in the long-term best interests of the nation; and currect data policies are fundamentally sound. This study came into fruition with the passing of Public Law 98-525 which paralleled many of the study conclusions. Unfortunately, Public Law 98-525 has not been fully implemented. Concerned with a lack of guidance in this area, the Joint Logistics Commanders (JLC) Panel on Government Data Rights was chartered in June 1985 to develop a comprehensive joint service program for the acquisition and management of technical data.

The final product of this JLC Panel will be a joint service directive establishing uniform procedures for technical data. Primary emphasis will be on the proper identification, specification, acquisition and enforcement of Government rights in technical data necessary for competitive reprocurement. Both Government and contractor interest and resources will be balanced in laying out a program to ensure that mismarked, missing or incomplete data will be detected prior to contractor delivery, while ensuring that contractors' valid proprietary data are protected.

General O'LOUGHLIN. The Air Force is currently reviewing acquisition policy in the Wheel and Brake area. The proposed policy is based on an extensive Wheels and Brake study conducted by AFLC and AFSC. Upon finalizing the policy, we will send copies to the committee.

General BABERS. It would be very advantageous to the Department of Defense if legislative provisions were made for a specific period of time, e.g., seven years from date of any contract, during which the Government would recognize, honor, and protect the valid claim of that contractor that only limited rights in data were transferred to the Government. During that time interval, the Government would agree not to disclose the data in question outside the Government for any purpose except in time of war or grave national emergency and only then if that contractor could not deliver sufficient quantities and quality demanded by the response to the war or national emergency.

Further, the Government would agree that during the specified time period, it would make no attempt to subvert the contractor's data by any means, e.g., reverse engineering unless the item(s) made using the data in question was subject to a price increase greater than the rate of inflation plus two (2) percent per year. After the specified time has elapsed, the Government must have full and complete rights to the data including the right to release it to any party, domestic or foreign, where the release serves the best interests of the Government.

Data currently in the possession of the Government or coming into the possession of the Government prior to the effective date of the above or in any way not subject to the above, should be deemed free of any restrictions, i.e. the Government has unlimited rights, beginning on the tenth anniversary of its delivery to the Government.

Such a situation affords the contractor greater protection than he now enjoys for seven years or the specific interval selected by Congress, as long as he did not take unreasonable advantage of his situation. Beyond that time, the Government can reduce costs, expand the production base and enjoy the benefits of competition by the use of Unlimited Rights to the data.

In today's rapidly unfolding scientific and technical environment, exclusive use of an idea, part, or process is unlikely to remain the province of any one person, company, corporation, or other entry indefinitely. This proposal offers a fair compromise between the rights of an individual (or other entity) and the needs of the people as a whole represented by the Government.

Thank you, Mr. Chairman.

Senator QUAYLE. Thank you, Senator Glenn.

I have one other request I would like to make. I wish you could take an aggregate or give some specific examples, preferably in the aggregate, and give the subcommittee a breakdown of what this legislation has done in the following areas: Cost savings, increased costs, increased delays, and any additional personnel assigned because of legislation.

[The information follows:]

General THOMPSON. I can tell you the effect of the acquisition reforms at an overall aggregate level for spare parts procurements as to leadtime, resources and savings. From fiscal year 1983 to fiscal year 1985, productivity is down 16 percent. During the same time, administrative leadtime for parts has grown by an average of 58 days at an estimated $10 million per day or $580 million (one-time). During fiscal year 1984 and fiscal year 1985, approximately 1,100 additional personnel were recruited to support the Spare Parts Initiatives. About 54 percent of those personnel are devoted to procurement and the remainder have been assigned to technical support. Estimated cost for the personnel increase over the 2 year period is $71 million. Cost avoidance saving during the same period from the AMC Spare Parts Initiatives is $567.OM. This includes savings realized from the Breakout Program, including breakout to the actual manufacturer and breakout to competition, recoupments, value engineering and consolidation of purchases.

I cannot segregate these effects by laws or regulatory requirements since we do not track to that level of detail. Moreover, any attempt to develop such a tracking system or to judgmentally allocate the information to specific legislative or regulatory revisions would be next to impossible and any attempt to do so would only render a highly speculative result.

One problem prohibiting the allocation of these statistics to their originating cause is their overlapping nature. This is due to the fact that many of the laws and regulations cover the same issue but one may have preceded the other, in some cases, or vice versa. Additionally, in many cases the promulgation of revisions are combined such that implementing directives cover both the legislative and regulatory revisions. Moreover, it is not simply the individual legislative or regulatory changes which are causing us to have negative impacts.

The collective impact of all the changes are resulting in the entire acquisition community presently being in a state of confusion, upheaval and frustration with no end in sight. The impact of this turbulence, combined with the increased reluctance of acquisition personnel to complete an action without repetitive and comprehensive review regardless of dollar value, is impacting lead-time and productivity to an immeasurable but real extent.

I should point out that this continuous state of change is also complicating our attempts to use automation to offset leadtime growth and productivity declines. Each change must be reviewed for impact on existing and proposed ADP systems. In many cases, changes to the existing ADP system is required and must take precedence over new automation efforts which are intended to increase the effeciency and effectivity of the acquisition process.

I don't want to give the impression that most of the legislative and regulatory revisions haven't been good. However, the sheer number and the contents of the revisions are causing in many cases, major procedural changes at our major buying commands. I think until "the dust settles," a moratorium on any further revisions is warranted except for those providing relief in the area of simplification and efficiency which will not impact on effectiveness gains.

Admiral HUGHES. Numerous Navy initiatives and legislative reforms enacted over the past few years have affected the acquisition and contracting process. While the specific effects of a single initiative or legislated reform in terms of specific cost savings, increased costs, increased delays or additional personnel requirements are unknown, our managment indicators for the Navy's procurement system show that each area has been affected. Specific examples are as follows:

a. Cost savings—The Navy's establishment of a Competition Advocate General in July 1983 preceded the competition in Contracting Act of 1984 (PL 98-369). Through fiscal year 1985, significant savings in excess of $2.5 billion have been realized in our ship building programs through competition. Competitive awards have increased from 26.7 percent in fiscal year 1982 to a record 44.1 percent in fiscal year 1985. Our goal for fiscal year 1986 is 51 percent of total procurement dollars. Navy initiatives in the spare parts area resulted in the creation of the Buy Our Spares Smart Program (BOSS) in August 1983. BOSS objectives are to increase breakout substantially, enhance opportunities for competition and eliminate the "clericalization" of the spares acquisition process. BOSS savings after expenses were $158 million in fiscal year 1984 and are projected to be in excess of $184 million for fiscal year 1985. Since 1982, savings attributable to multiyear procurement exceed $750 million.

b. Increased costs—There are increased costs associated with both legislated an regulatory reforms. Unless the initiative is separately budgeted and monitored, the specific cost of a given initiative is not known. For example, the transition from the Defense Acquisition Regulation to the Federal Acquisition Regulation (FAR) and DOD Federal Acquisition Regulation Supplement was disruptive and costly. Additionally, to make FAR changes requires approval of the entire FAR Council, representing *all* government agencies. This process is inordinately time consuming and inefficient. Also, resources for the BOSS Program cost $101 million for fiscal years 1984 and 1985, while total cost savings for this same period exceeded $338 million. Multiyear contracting has the potential for significant savings over single year contracting.

Appropriation Act limitations in 1984 and 1985 prohibited such contracting for a major system unless the Appropriations Act specifically provided for it. Also, the prohibition of hybrid contracts (contracts wherein recurring costs are included in the cancellation ceiling to protect the contractor's investment of its own funds in Economic Order Quantity) has potentially lost savings. The provision of the fiscal year 1985 Authorization Act adding 10 U.S.C. 2321, validation of proprietary data restrictions, is expected to increase costs significantly. The provision requires a final disposition of disputes regarding the validity of restrictive legends before the legends can be struck. Thus, contractors can delay the use of the data for competition by engaging in protracted litigation.

c. Increased delays—the Navy has experienced an increase in our procurement administrative lead time (PALT) for purchases over $25,000. Lead times have grown from 88 days in fiscal year 1983 to 112 days in fiscal year 1985 for these large procurements. Increased delays result from such legislated requirements as the COC referral to SBA required for *all* nonresponsibility determinations regardless of dollar value; the expanded synopsis requirements; and the current threshold for requiring costs or pricing data. Increasing PALT results in growing costs of inventories and decreased operational capability.

d. Additional personnel—Through the end of fiscal year 1985, we have dedicated 735 additional civilian personnel under the BOSS Program.

A breakdown of this civilian workforce is as follows:

Procurement specialists	238
Engineers and engineering technicians	125
Personnel in procurement assistance roles	111
Personnel in BOSS assistance roles	261

Resources to maintain the momentum of BOSS have been programmed to rise from the 550 end-strength and $35 million allocated in fiscal year 1984, to over 1,000 end-strength and more than $100 million in fiscal year 1988. This level of investment guarantees high interest in the program and close scrutiny of the results.

The Small Business Administration Breakout Procurement Center Representative and technical advisors, required by Public Law 98-577, is another resource with additional associated costs to the Government.

General **Skantze**. Legislation has impacted us in a number of ways. Procurement lead time continues to increase. For example, within the Air Force we have added an additional 30 days to the procurement lead time for justification and approval of those contractual actions in excess of $10M that are categorized as "less than full and open competition." To date there has been no value added.

Synopsis lead time has also increased procurement lead time. Synopsis of a follow on weapon system where there is no possibility of dual sourcing does not make sense. We should be able to issue a Request for Proposal without waiting the 15 day period.

Productivity has been lost due to a plethora of changes. Further, morale of the acquisition workforce is at its lowest point due to continual negative publicity. We are having a tough time filling our acquisition vacanies with qualified personnel. Last year AFCMD experienced a 25% turnover of civilian personnel. It's difficult enough trying to ensure delivery of quality weapons systems when you are 100% manned and extremely difficult when you are only 75 to 80% manned.

The changes as a result of CICA are not yet fully understood at the grass roots level. The past six months we have received over 500 inquiries regarding the application of this statute to specific acquisitions. As a result, we have established another two day workshop in December 1985 to conduct further training. Over 200 problematic questions have been submitted by the field for resolution and guidance at this upcoming training seminar.

It is due to these types of impacts that we need a moratorium on new procurement legislation. We have to let the system settle down to truly assess where we are before we can determine where we need to go.

General **O'Loughlin**. Because of the complexity of acquisitions in AFLC, there is not a simple answer to these questions. Addressing each of these:

1. Cost Savings. All of the initiatives taken to improve spares acquisition in AFLC resulted in an overall cost savings (avoidance) of $529 Million in Fiscal Year 84. This was computed by comparing unit prices for items bought in FY83, multiplied by the quantities purchased in FY84. For the first 9 months of FY85, these savings, or cost avoidance, amounted to $519 Million, again using FY83 prices as a base and comparing them to FY85 prices. These savings occurred because of four reasons. First, adeqate spares funding allowed us to purchase spares in more economic quantities. Previously, because of funding shortfalls we bought the same part two, three,

and often four times a year. We now purchase annual quantities, increase the quantities purchased when we can achieve a major price savings, and even purchase multiple years' quantities when it is cost-effective to do so. Second, we have made a dedicated effort to breakout the purchase of spares from prime contractors to actual manufacturers. Most prime contractors have been very cooperative in identifying actual manufacturers in this effort. Third, we have greatly expanded our capability to purchase spares in a competitive environment. In FY84, over 12,000 spare parts were coded for competitive purchase for the first time and in FY85 another 14,000 parts were coded for first time competition. Finally, our personnel have simply been better negotiators of prices when we are in a sole-source buy situation. Better support of the prices of parts has been required, we have used detailed government estimates of should-cost more extensively, and our negotiators have simply been tougher at the negotiation table. All four of these factors have operated synergistically in our system and the $1,048 Million cost avoidance we have achieved in the 21 month period with the result of all of these factors. The order the factors was discussed is our assessment of their relative contribution.

2. Additional personnel and increased cost. To improve our system, we added 750 new personnel authorizations in FY84 and 2,426 new authorizations in FY85. Most of them (1,330) were added to improve our capability to breakout and compete items. 560 new authorizations were added directly to the contracting workforce in AFLC. The total additional personnel costs for this was $23.4 Million in FY84 and $68 Million in FY85. Another major cost element experienced in the wake of changes to the acquisition process was the large amount of overtime our personnel had to work to accomplish the new, manpower-intensive tasks imposed on them. In the AFLC contracting activities, alone, we spent almost $3.2 Million for overtime pay in FY84 and over $4 Million in FY85. This was almost 5 times as much as we spent in the same offices in FY83. The major "cost" of the changes we have made is seen in the increase in pipeline time covered by the large increase in administrative lead time.

3. Increased delays. The entire process of spare parts acquisition has been slowed because of these changes. The following date reflects our average Contract Administration Leadtime (CALT) which reflects the time required from receipt of a requirement in our contracting offices until it is on contract. The CALT grew from 60 days in Oct 82 to 76 days in Sep 83, 106 days in Sep 84, 116 days in Sep 85, and 133 days in Apr 85. This growth occurred because of a number of factors operating in the acquisition arena. These factors can be summarized in the following categories:

(a) *Legislative changes.* There were some direct changes made in the laws which caused delays in the acquisition process. Public Law (PL) 98-72 which mandated a 15-day waiting period between publication of a synopsis and issuance of a solicitation and a 30-day waiting period from solicitation issuance to proposal receipt or start of negotiations expanded CALT. Similarly, the sole source justification requirements of that PL, and later the Competition in Contracting Act (CICA), extended these lead times. Another provision of CICA extending CALT was the requirement to obtain certified cost and pricing data to a lowered threshold of $100,000. The very active legislative arena which produced PL 98-72, CICA, PL 98-577 and PL 98-525 was a part of the overall environment affecting AFLC acquisition.

(b) *Change itself.* Not only were there major legislative changes during this past two-year period of time, but there were even more administrative changes. In May 83, the Air Force formed an Air Force Management Analysis Group (AFMAG) to totally review the spares acquisition process. The AFMAG final report issued in Oct 83 had 178 specific recommendations for changes leading to improvement. Virtually every one of these changes have been made. The adaptation to all of these changes has created a most difficult environment to work in and has been responsible for much of the increase in CALT.

(c) *Pricing changes.* To eliminate the distortions of prices we had seen in the past, individual prices of all items down to the lowest unit-priced items have undergone extensive examinations. In addition, where we previously negotiated only the "bottom-line" of contracts which had a number of specific line items, we now subject each of them to a detailed review to insure the price of each item is reasonable. All of this has slowed the process.

(d) *Manpower.* While we have expanded our manpower base considerably, this expansion lagged the implementation of the changes we made in our process. In the last two years, AFLC has hired over 900 new contracting personnel with over 93 percent having college degrees. Each of these employees, hired under a program we call PACER PRODUCE was given over 90 days of extensive training prior to starting work. The success of this program is now being seen throughout the Command.

(e) *Psychological.* The major reason for the almost paralysis of our acquisition process is the psychological one. No one, government employee or contractor, wants to be associated with the new so-called "horror" case. This psychological impact is seen in all phases of the procurement cycle—longer times for contractors to propose prices, longer time for audits, longer times for field reviews, and longer review, analysis, and negotiations by our buyers and contracting officers. The fear of any error and the desire for a perfect, 100 percent, system has had a major impact on our process.

General **BABERS**. The Defense Logistics Agency's breakdown of cost savings and increased costs as a combined result of the 1984 reform legislation and DLA management action is provided below. We cannot segregate the cause of the savings and the costs. All dollar figures are in millions.

Savings accrued from Spare Parts, Competition and Pricing Initiatives by DLA Purchasing Activities are as follows:

[In millions]

	Fiscal year—	
	1984	1985
Value engineering	$75.60	$98.37
Replenishment spares breakout (estimated)	3.50	13.20
Overpricing refunds	.68	1.47
Other competition and pricing initiatives	43.20	54.65
Total	122.98	167.69

Cost avoidance as a result of the Standardization Management Program is as follows: FY 84, $139.10; FY 85, $109.30.

Total Investment (Cost) FY 84, $13.80; FY 85 (Estimated) $36.50.

Total Investment includes personnel, automated data processing equipment, program, and other support investments. It should be noted that personnel investments for Defense Contract Administration Service Activities in support of Military Services Programs are also included. Savings from these activities primarily accrue to the Military Services and not to the Defense Logistics Agency.

Net Savings (Less Cost Avoidance and Investment): FY 84, $109.18; FY 85, $131.19.

Additional personnel assigned from FY 83 thru August FY 85 were as follows:

Contracting	811
Contract management	454
Quality	460
Total	1,813

Increased delays resulting from legislation are described in my formal statement. Increased delays since 1983 resulting from DLA management action are as follows:

PROCUREMENT ADMINISTRATIVE LEADTIME INCREASES SINCE 1983 RESULTING FROM DLA MANAGEMENT REQUIREMENTS

Activities affected	Management requirement	Number of days
Hardward centers	Headquarters review of priced orders under a nonprepriced basic ordering agreement (BOA).	[1] 13
Do	First time buys valued not over $1,000 must be processed through our competitive automated purchasing system or made manually rather than by our rotating blanket purchase agreement automated system.	[1] 60
Do	Approval of priced BOA orders and definitizations	[1] 1
Hardware	Reasonable evaluation of alternate spare part offers	[1] 10–60

[1] When applicable.

Senator **QUAYLE**. In that you are also going to have to break it down on what you have done in the area of additional personnel cost, cost savings in response to legislation and also in response to your own service regulations because I think there are some internal regulations that have imposed additional costs, additional delays, et cetera.

So, you are not going to be able to lump this all together. You have to spread this out. This goes to the heart of the problem we are talking about.

If you could get that data, cost savings, additional cost, delays, additional personnel, statutory and regulatory, it would be a great benefit to this committee in its oversight responsibility which we are trying to undertake.

With that small meager assignment, does anybody have any final comment?

General **SHANTZE**. I would like to repeat something I said before.

I think it is absolutely imperative that this subcommittee be a focal point for procurement legislation. I think a lot of comments you have heard have been comments on redundant legislation and conflicting legislation.

I think in the way the amendments are proposed in the Congress, if there were some ombudsman, if you will, for procurement legislation who could say, well, this will conflict with that or this does not match with that, a lot of the problem would be handled at that level.

I just think it is a willy-nilly process of throwing amendments in the hopper without any consideration whether they all fit on not.

Senator **QUAYLE**. The only thing I can assure you is that this subcommittee and this committee will be the focal point for substantive legislative proposals. Any legislation that deals with procurement for the military will come to this subcommittee.

That has not always been the case. That is why the subcommittee has been created. It has been in existence a little over 2 years now. Unfortunately, amendments are offered on the floor, and things of that sort, which we cannot control.

We have a small problem we have to work on right now. I understand the House Appropriations Defense Committee has added a bunch of statutory legislation which we knocked out and compromised in the conference. We will have to fight that battle over again and see how we are going to be able to knock it out in the conference again because they had no authority to do it in the beginning.

With that and before we go any further, thank you very much and we look forward to your response.

[Prepared statement by Rear Adm. Stuart Platt follows:]

PREPARED STATEMENT OF REAR ADM. STUART PLATT, SUPPLY CORPS., U.S. NAVY, COMPETITION ADVOCATE GENERAL OF THE NAVY

INTRODUCTION

Good morning, Mr. Chairman. I am Rear Admiral Stuart Platt, the Competition Advocate General of the Navy. I am pleased to testify for the Navy today on the 1984 defense procurement reform legislation. My responsibilities include the development, evaluation, and management of competitive strategies in Navy and Marine Corps procurement, so my testimony will address 1984 procurement legislation from that perspective. The Navy has been at the forefront of recent-year Defense Department efforts to increase procurement competition. We are grateful for the opportunity to share our experiences with your subcommittee.

STATUS & IMPACT OF 1984 DEFENSE PROCUREMENT REFORM LEGISLATION

Prior to congressional discussions of the Competition in Contracting Act of 1984, the Navy was instituting major changes in the way we do business. Navy efforts to make competition a cornerstone of its acquisition strategy reached a turning point in July 1983 when Secretary of the Navy John Lehman established the flag officer position of Competition Advocate General. I am honored to have served as the Navy's first Competition Advocate General during this period, which has also been a period of our major buildup to a 600-ship naval force. We have diligently sought the highest return from the investment of taxpayer dollars, and we have succeeded in achieving significant savings. Competition and firm fixed-price contracting are the foundation of our cost-control policy. Our initiatives to follow sound business practices have not come at the expense of readiness. Our military readiness is high, as we demonstrated in the skies over the Mediterranean!

The sheer magnitude of the Navy's thrust for increased competition in the defense marketplace is impressive. By raising competition from 26.7 percent in FY1982 to 44.1 percent in FY1985, we competitively awarded $10.8 billion more than we did three years ago. We expect the trend of steadily growing competition to continue. We have set our competition goal for FY1986 at 51 percent—approximately double the level achieved in FY1981 and FY1982.

When we reach the point where over half of our procurement dollars are awarded competitively, we believe there will be a synergistic effect. The cost-sensitive management we all seek will become evident even in the business practices of sole-source contractors. Competition should motivate our defense firms to trim corporate "fat" and invest in productivity enhancements, which should improve the posture of American industry in the increasingly competitive world marketplace.

This chain reaction from competitive awards can create an increasing climate for excellence.

The Navy's considerable experience with competition in contracting has been most favorable, largely due to the personal attention of the Secretary of the Navy and the Chief of Naval Operations. A few years ago, there were some individuals and organizations who believed, and hoped, that our program was just a passing trend. However, they misjudged the determination of Navy leadership and refused to accept the possibility that prices of defense systems and equipment could be reduced. They also failed to recognize the daily announcements of competitive awards flashing before their eyes as indicators of a change in the way Navy conducts its business.

Problems and successes in the defense business have made headlines in newspapers and magazines in recent months. Many of the problems are found in firms which traditionally have been the recipients of large sole-source contracts. It is not the practice of leaders of these firms to step aside when a serious failure occurs. I am not advocating such a step, but I am suggesting that large problems in industry demand appropriate action. I am pleased to see a growing trend in this country toward ethical business practices and acceptance of accountability in management.

The Navy reemphasized competition not for competition's sake but for the lower prices, higher quality, and stronger industrial base which it provides. We continue to see savings from our competitive procurements, and these savings help us accommodate the costs of our growing fleet. Competition has improved the quality of systems. Contractors tend to put their best people on their competitive contracts, and the result is higher quality work. A major aerospace contractor tells me a person on the shop floor works harder when the employee knows there is someone on the shop floor of a competitor's plant doing a similar job.

The Navy supported the Competition in Contracting Act of 1984, which requires justifications and approvals of non-full and open competition procurements. This provision and the requirement for command competition advocates to approve procurements valued between $100,000 and $1,000,000 have enhanced the effectiveness of the Navy and Marine Corps competition advocates. Our commanders and commanding officers are fully aware of their responsibilities for good business practices, so the role of their competition advocates—especially in systems commands and other large procuring activities—is becoming increasingly important.

The Competition in Contracting Act sent an important message to the defense acquisition community. Managers and executives throughout government and industry are realizing that competition is not only the Navy's preferred business practice but also the law of the land. It is here to stay. The Navy has succeeded in bringing about a major change in behavior. We believed that what we planned would be hard to do, but we were convinced it was right. We approached our task with the intensity of that conviction.

Our experience demonstrates the value of a central focal point for competition in each Service—the Competition Advocate General, now established in law. My responsibilities include review of all noncompetitive procurements over $10,000,000 in value and review of acquisition plans for all major programs. I make recommendations regarding competition to the Assistant Secretary of the Navy for Shipbuilding and Logistics, who has final authority in his role as Navy senior procurement executive. This process allows the Navy's civilian leadership to exercise control over the long-range business planning for major acquisition programs and helps ensure that competition is planned for early in each acquisition. Incidentally, the disestablishment of the Naval Material Command earler this year eliminated an organizational level of bureaucracy. The transition to a streamlined naval material establishment, wherein system commanders have direct accountability to the Secretary of the Navy and the Chief of Naval Operations, has worked well to date.

In my view, Navy program managers, contracting officers, and systems commanders are incorporating effective competition plans in their acquisition strategies and procurements. My staff conducts an in-depth review of each competition plan, and I have been able to recommend approval of all but 25 percent of the documents submitted. For the remainder, I have recommende either disapproval or conditional approval subject to specific actions to increase competition. Now that Navy managers and executives are accepting competition as the normal way of doing business, the rate of rejection should decrease substantially.

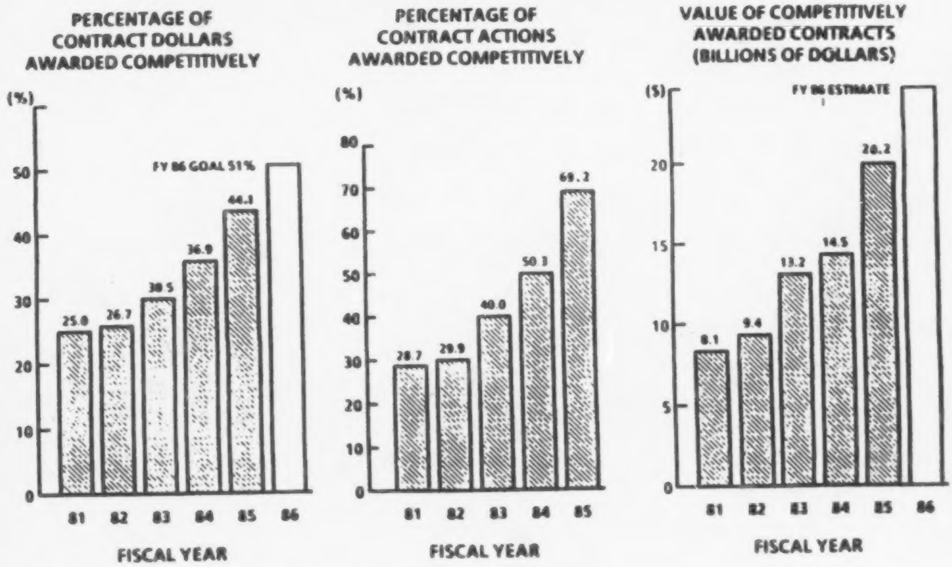
We are continuing to sponsor research efforts to improve our understanding of defense competition. Specific efforts include expanding our competition data base and refining our cost/benefit analysis models. Past cost analyses did not accurately forecast savings from competition, yet every Navy program that has been dual sourced has generated net savings. One Navy study has shown that profitability at major defense contractors is higher in their government work than in their commercial work. We have also observed that some firms use cash accumulated from defense business to purchase their own stock, to retire their long-term debt, or to buy other companies This is a complex subject which requires careful analysis. One thing is clear, though: steps taken by defense firms to invest in technology and improve productivity on plant floors will benefit the nation.

You may be interested in talks I have had with the Chief for Defence Procurement of the United Kingdom's Ministry of Defence. Although this is not necessarily a reinforcement of our solution to defense procurement problems, the United Kingdom has announced that competition will be the primary way of doing business for the military. This represents a dramatic change for them. I understand their new approach is to seek, at minimum, limited competitions between two or three qualified suppliers. Our experience has been that seeking an infinity of competitors is often a waste of time, and the concept of more limited competition—as we use in major shipbuilding programs—is worthy of consideration. Auditing of defense contracts in the United Kingdom and in the United States has risen significantly. We fully expect that the necessity for auditing will level off as competition and fixed-price contracting continue to increase.

DEPARTMENT OF THE NAVY COMPETITION RESULTS FOR FY1985

Secretary Lehman's leadership has established a climate which encourages excellence in procurement. His emphasis on cost-sensitive management of acquisition programs and his advocacy of competition are widely known. The Navy's sharp increase in competitive awards could be described as one of the most dramatic turnarounds on the American business scene in recent years. Forty-four percent of FY1985 contract dollars were awarded competitively. The value of FY1985 competitive awards was $20.2 billion, more than twice the amount of FY1982 awards. Sixty-nine percent of FY1985 contract actions were awarded competitively, more than double the level in FY1982. The following three graphs show the year-by-year improvement that has occurred.

DEPARTMENT OF THE NAVY
PROCUREMENT COMPETITION PERFORMANCE



BREAKDOWN OF NAVY COMPETITION BY INDUSTRY SEGMENTS

The Navy's policy is to compete all new starts, commencing with the design phase, and to carry competition forward through full-scale development and production—to the extent that it makes good business sense. For existing programs, our policy is to establish second production sources in every appropriate program. Following is a brief summary of how we have carried out these policies in our major markets.

SHIPBUILDING

The percentage of shipbuilding dollars awarded competitively has increased from 15.7 in FY1980 to 84.3 in FY1985. Virtually all shipbuilding programs are now competed except the Trident submarine program. We are taking steps to rectify that situation, and I see a viable potential for future competition in the Trident submarine program. The impressive savings of $2.5 billion from shipbuilding competition during FY1983-1985 include $248 million in the SSN 688-class nuclear attack submarine program and $840 million in the CG 47-class Aegis cruiser program.

AVIATION

We have made good progress in creating and sustaining competition in our aircraft programs. Our newest aircraft, the V-22 Osprey, is being developed for the Marine Corps by a team of two major contractors, each of which will compete for the larger share of annual production contracts. We plan the same approach for production competition in our advanced tactical aircraft program, whose design will be fully competed. In our competition for the inner-zone CV helicopter program, we awarded a fixed-price development contract with priced options for five production lots. We project a savings of $1.5 billion in total acquisition cost compared with our initial estimates based on sole-source procurement.

We are establishing Pratt & Whitney as the second source for the production of General Electric's F404 engine used on the Navy and Marine Corps F/A-18 strike fighter. In the support equipment area, we are establishing second production sources for three families of automatic test equipment, and we are competing the test program sets for these systems. We project savings of $334 million over five years from the test program set competitions alone.

COMBAT SYSTEMS AND WEAPONS

We are working on establishing second production sources for the Phoenix missile, Standard missile II, and RAM (rolling airframe missile). FY1985 was the first year of head-to-head competition between McDonnell Douglas and General Dynamics for the larger share of production of Tomahawk cruise missiles. We are establishing second production sources for the major subsystems of the Aegis combat systems, and we are developing a second source for Aegis integration and testing. We have established a second production source for the vertical launching system for shipboard missiles; in FY1985 we saved $55 million as a result of competition for this system. I recently recommended establishing a second production source for the Phalanx close-in weapon system, which will be installed on many combatant ships.

ELECTRONICS

Savings achieved by competing electronics equipment and maintenance have been noteworthy. The competition for the acoustic array of the SQR-19 sonar system should produce a savings of some $165 million. In the competition for operation and maintenance of simulators, man-year prices were reduced from $55,000 to less than $25,000. The Marine Corps competed the repair of travelling wave tubes and discovered the traditional contractor had been subcontracting the work to another vendor. We project an annual savings of $168,000 based on a competitive price of $5,950 per repair and a previous sole-source price of $19,958.

COMPONENTS, EQUIPMENT AND SPARES

Spare parts procurement is an important issue, and pricing problems are getting the attention they deserve. The Navy's "Buy Our Spares Smart" program consists of initiatives designed to increase competition and ensure that we pay no more than fair and reasonable prices for spare parts. The Navy is on the right track, and the thousands of competitive contracts being awarded daily by dedicated Navy professionals is a real solution to overpricing. Largely due to competition, replenishment spares bought in FY1984 cost 12 percent less than the same items bought during the previous year, and similar results are expected for FY1985.

As an example of competition savings in the spares area, the Navy competed requirements this year for external fuel tanks for the F/A-18 strike fighter; the winning firm bid approximately $12,000 per tank, which contrasts with the previous price of $57,130 paid to the sole-source supplier. In another case, the Marine Corps held their first competition for mobile tool cabinets, and a new competitor bid $721 each versus the previous sole-source supplier's price of $1,400; estimated savings for this procurement total $150,000.

SERVICES

We have emphasized competition in support services contracting because competition should logically dominate this area. The Navy established separate competition goals for support services contracting in FY1984, and we continued that practice in FY1985 and in FY1986. Competition levels have more than doubled over the past three years: competitively awarded dollars increased from 29 percent of total contractor support services dollars in FY1982 to 60 percent in FY1985.

In a related area, the Navy and the other military departments have agreed to conduct a joint competition for ground support services and maintenance of C-12 utility aircraft. We expect this will be a real cost saver because at least six qualified firms have recently competed in competitions that yielded savings on similar work for two other Navy aircraft.

CURRENT COMPETITION OBJECTIVES

The foregoing gives an indication of how we are rationally harnessing the market forces of competition to the benefit of the Navy and the taxpayer. There is more that can be done. We are pursuing objectives to intelligently increase competition further. Some examples of these initiatives are described below.

SPEED UP CONTRACTING PROCESS

There is a concern among some that our contracting process is frequently too lengthy. We are including production options in contracts whenever appropriate so that these competitively awarded options can be exercised in future years without having to go through another competition. We are looking for ways to simplify and speed up the process so that competition does not delay program schedules. Except when we use a sealed-bid procedure, negotiations generally take some time whether we are using competitive source-selection procedures or noncompetitive procedures. For example, one of the last ship construction contracts awarded in FY85 was for a Trident submarine, a sole-source award which was delayed while we assured ourselves of the reasonableness of the price.

Since we conduct business on a full-disclosure basis, we presume we are dealing with knowledgeable sellers, and we hope to do away with the stalling which can delay the negotiation process. Contracting officers and supporting offices are being tasked to do a more thorough job of specifying the government's requirements. They are on guard to stop firms from submitting marketing brochures in place of well-though-out proposals. We are considering the use of standard forms to aid us in source selections. We are asking our contracting officers to hold discussions with prospective offerors at bidder conferences about upcoming procurements and to involve them to the extent practical in helping review requirements. This should reduce the use of needless best-and-final offers and should decrease the time required for give-and-take between the government and industry.

The experience our contracting officers are gaining in competitive acquisitions will help them develop improved competition strategies and will speed up the contracting process because less time will be lost to the effort required to modify business planning. Additional training in competitive acquisition is one of the most effective actions we will continue to pursue, for we are essentially reorienting an entire Navy procurement workforce to overcome the vestiges of the institutional bias in favor of sole-source procurement which previously existed. This needed to be done and is being accomplished. We believe that at many of our procuring activities, we should train our buyers to be specialists rather than generalists. Purchasing along product lines should improve the quality of our procurements.

OBTAIN NECESSARY TECHNICAL DATA AND RIGHTS IN DATA

The lack of reprocurement technical data or rights in that data at times remains a barrier to full and open competition.

We are emphasizing the need for early planning to obtain technical data so that competition in production is possible. We fully recognize the benefit of innovation to the nation and the need for protection of inventions and trade secrets. However, the area of data rights is not an exact science. We believe the government legitimately owns more rights in data than industry associations indicated last year when technical data legislation was being considered. We have to present the facts clearly as we work with contractors who claim proprietary rights in data which we question. We are initiating court cases when we believe such action to be justified. Our aim here is only to assure we can obtain, when needed, data we have already paid for.

The following examples demonstrate our success in removing technical data barriers to future competition for specific systems.

O AN/APS-137(V) P-3C RADAR—the system manufacturer claimed proprietary data rights, which prevented us from competing a $490 million radar production program. After discussions, the firm submitted a revised proposal which provides unlimited rights to the government without charge.

O AN/SAR-8 INFRARED SEARCH AND TARGET-RECOGNITION SYSTEM—the subcontractor for the electronic heart of the system, a spatial processor, offered to sell unlimited rights for $176 million. After discussions, the firm agreed to transfer without charge the rights necessary to implement the Navy's second-sourcing plan.

O ENHANCED HIGH-SPEED E-2C SIGNAL PROCESSOR—the company which manufactures the current signal processor initially claimed proprietary data rights, which would have precluded competition in production of the enhanced processor. The contractor subsequently agreed to provide the rights required for second sourcing without charge.

INCREASE SUBCONTRACTOR COMPETITION BY SOLE-SOURCE PRIME CONTRACTORS

Competition makes good business sense for the majority of our contracts. These are, of course, cases where we must contract on a sole-source basis. Here, our goal is to receive the best value: high-quality products at a fair and reasonable cost. We have changed our method of contracting by moving from cost-plus to firm-fixed-price or fixed-price-incentive contracts. These give contractors the incentive to control costs and improve productivity. We also work to achieve the lowest possible cost by insisting on maximum feasible competition in subcontracts awarded by the prime contractor. This is important because subcontracted work and purchased parts often account for more than half of the total contract price. When appropriate, we are requiring a specified level of subcontractor competition as a part of prime contracts.

In a recent report, the General Accounting Office noted that prices tended to rise when prime contractors stayed indefinitely with one supplier or with a limited number of suppliers. I was pleased when some of our largest prime contractors (General Dynamics was the latest) advised us of the appointment of corporate competition advocates, whose responsibilities include seeking increased subcontractor competition. These actions by industry, if they increase secondary competition, are welcomed by the Navy.

ELIMINATION OF "GOLD PLATING"

The Navy has started a drive to streamline specifications and standards. To spearhead this major effort, the Navy has established the position of Specification Control Advocate General of the Navy and appointed a member of the Senior Executive Service to fill the position. We can expect improved opportunities for competition as we are able to eliminate unnecessary specifications and standards, so this important initiative has top-level Navy support.

CLOSING

In summary, the Navy's increasingly competitive environment is helping us work out feasible solutions to the problems of affordability. We are concentrating on obtaining the "best value" in our procurements. Competition is driving prices down and improving quality. There is a new attitude and acceptance of competition by program managers, and there is a recognition by industry that the Navy is deadly serious about competition and about reducing the cost of its goods and services.

Competition has become a way of life in the Navy. We are carrying out this change on a national basis. The compliance reviews in my office and in those of competition advocates at buying commands throughout the Department provide the necessary checks and balances to a system which was inclined to go in another direction. Even the threat of competition has motivated sole-source contractors to improve cost control and offer lower prices, as we observed when we initiated second-sourcing efforts for the HARM (high-speed anti-radiation missile). During this same period of time, we have remained firm in expecting quality goods and services; this is always a paramount concern.

Support of the top Navy leadership and the Congress has been crucial to the success of our competition program. I cannot overemphasize the value of top-level support. I see this support as the key ingredient in the Navy's formula for success.

The Competition in Contracting Act of 1984 has certainly had an immense impact. It establishes competition as the baseline contracting approach—a major Navy objective for several years. We now have fewer procurement problems and nagging claims. The massive changes we instituted are, in my view, working for the benefit of the Navy and the taxpayer. I believe we have done the right thing for the country. In my view, it would be proper to hold further legislation in abeyance until the full effect of 1984 legislation is known. I can assure you we are taking the reform already set in place seriously and will take firm additional steps if necessary to obtain quality and reduce costs.

Thank you for the opportunity to present the views of the Navy from a competition perspective and to discuss how we are increasing competition in Navy and Marine Corps procurement. I will be pleased to answer any questions you may have.

[Questions with answers supplied follow:]

QUESTIONS SUBMITTED BY SENATOR DAN QUAYLE

ESTABLISHING REVISIONS

Senator QUAYLE. General Skantze, list for us any other problems with statute not already covered in this hearing that the subcommittee should be looking at; specifically, what should be considered for repeal or modification and why.

General SKANTZE. I would like to raise several issues. Current Warranty legislation under P.L. 98-525 limits our available acquisition strategies and increases costs. Warranties are but one tool considered during the development of an acquisition strategy to attain our performance and supportability objectives. It does not make sense to require warranties for many satellite and missile systems. We clearly need increased flexibility; therefore, I strongly recommend that warranty waiver authority be vested in the Head of the Contracting Activity and that performance incentives be used in lieu of warranties when appropriate.

Additionally, the ability of our field people to "break-out" components, subsystems, support equipment, etc., is seriously hampered if the value is in excess of $10M. Competition in Contracting Act requires a new Justification and Approval if we are unable to compete. The law should be amended to allow break-outs when the data is not yet available for competition. Clearly, a "class type Justification and Approval" or an 8th exception should be incorporated into P.L. 98-369 to facilitate early break-out of spares and support equipment.

ADDITIONAL PROBLEMS

Senator QUAYLE. General O'Loughlin, list for us any other problem with statutes not covered in this hearing that the Subcommittee should be looking at; specifically what should be considered for repeal or modification and why.

General O'LOUGHLIN. The following sections of the FY86 DOD Authorization Act will negatively impact AFLC.

Section 911, Allowable Cost, will increase the lead time of covered contracts. A PCO cannot resolve questioned costs until he has both "adequate" documentation on the cost(s) and the opinion of the DCAA auditor. Also, this section requires "to the maximum extent practicable", the DCAA auditor be present at negotiations or meetings with the contractor regarding a determination of indirect cost allowability. Contractor certification on allowability is required, and, "to the maximum extent practicable", the regulations will apply to all subcontractors.

We can expect lengthy delays in dealing with our major contractors. PCOs will exercise more caution, incurring more delays, and DCAA's involvement will expand to cover all subcontractors, adding more time to proposal reviews. The size of the problem will be largely dependent on any additive restrictions imposed by the DOD issued regulations.

Section 912, Multiple Sources, requires all major defense acquisition programs provide for competitive, alternative sources from beginning of full scale development (FSD) through the end of production. This applies to both system and major subsystems. The Secretary has limited waiver authority. This section is effective with the first request for FSD fund for a FY after FY88.

Our major concern is that the section requires competitive, alternative sources if the systems serve similar functions. This presents us with an interchangeability/compatibility problem especially in complex weapon systems.

Unless, very carefully implemented, this section will impact our logistics function. Without guaranteed interchangeability, we could be forced into multiple sole-source arrangements during follow-on spare parts procurement. Finally, it will create a logistics management nightmare relative to field maintenance and tooling because a fielded weapon system could require up to double the existing amount of test and other support equipment.

Section 913, "Creeping Capitalism," was modified during the House/Senate Conference. Originally, the House wanted a mandatory 5% annual increase in competition, until 70% of the total dollars awarded was done competitively. The conferees agreed to require the SECDEF to establish FY goals and report progress to Congress annually.

Our concern with this is twofold: first, our ability to meet the goal which the Air Staff will levy on the Command, and secondly, the strong feelings expressed by the House sponsors of the original amendment to reopen this issue if they believe the SECDEF goals are not met. Mandating competition for competition's sake could result in stopping the DOD acquisition process or in awarding contracts to marginal performers whose delivered goods will also be substandard. Competition on a given part is both a business and a technical decision. We must continue to have the latitude to purchase times under other than competitive means when mission support and particularly safety demands this.

Section 914, Spare Parts Reform, requires the SECDEF to report to both Armed Services Committees on the actions being taken, with evaluation thereof, for the management problems which led to unreasonable spare parts prices. If the SECDEF determines problems have not been solved, he will issue regulations or propose legislation to fix problems. The report is due by 31 January 1986. Our concern is that 31 Jan 86 is too early to complete an assessment of our capabilities when we are still implementing new laws. Also, the Packard Commission Report on procurement activity is due by 31 Dec 85. With involvement from the Competition Advocate, GAO investigations, DOD IG reviews, the Packard Commission recommendations, and other influences, i.e., FY86 DOD Authorization Act, the Secretary's report will not be able to accurately portray the existing system vis-a-vis the 'better' system.

Under Section 918, Contracted Advisory and Assistance Services, Congress has directed the SECDEF to issue a regulation defining what services will be considered advisory and assistance services. All of the following must be considered: management and professional services; special studies; management and support services for R&D activities; training; management review of program funded organizations; public relations; other consulting services; engineering services relating to R&D; technical assistance; quality control, testing, and inspection services; specialized medical services; architectural and engineering services, other than construction; technical and management assistance for weapons system management and review.

DOD budgets sent to Congress will be required to identify the total amount of contracted services as delineated above, in terms of total dollars, by category, by service.

The potential impact to AFLC resides in the large number of engineering services contracts we issue for sustaining engineering. These contracts will no doubt be identified as either technical assistance, quality control, or technical and management assistance. Once the appropriate category is established, the new budget submission requirements will receive increased centralized Congressional control over these specific budget items. This continues the movement of Congressional control from oversight to micromanagement. The end result will be that Congress, not the user, will make the priority determinations on which program(s) receive continued engineering support from the weapon system design contractor. Of all the new requirements in the FY86 Authorization Act, the potential problems to the Command which this section could create are probably the greatest.

Section 924, Management of DOD Procurement Personnel, deals with specific education, training, and experience factors for program managers, general officers, and quality assurance (QA) personnel. Our concern is with the qualification restrictions which SAF must prescribe for general officers, which will be effective in 1990. SAF is the only waiver authority. This is another example of micromanagement by Congress.

However, of greater concern is the potential cost and lead time impact which the QA requirement will have on our Air Force Contract Maintenance Center (AFCMC). Having a mandatory attendance to a 4-week course within the first 6 months of assignment will compound the already long lead time problem AFCMC has in hiring for overseas assignment, which is currently about five months. Also, the DOD regulation must be issued ASAP so the courses can be established, curriculum developed, trainees scheduled, etc. 1 Jan 87 is not that far away.

The revolving door issue was addressed in the three separate sections: 921; 922; and 923. Congressional intent was to totally slam the door on preceived abuses of the public trust. These sections will make it harder for all of DOD to attract and retain qualified personnel, including senior acquisition experts. Finally, Section 934 holds the contractor liable for interest charges on overpayments based on contractor's submission of inaccurate, incomplete, or noncurrent cost and price data; even when unknowingly done. This will cause contractors to incur longer delays in submission of this data, and potentially even more voluminous submittals which will necessitate longer periods of review by both DCAA and field pricing analysts.

STATUTORY REQUIREMENTS TO CONSIDER FOR REPEAL OR MODIFICATION

Senator **Quayle**. General Babers, list for us any other problems with statute not already covered in this hearing that the Subcommittee should be looking at; specifically what should be considered for repeal or modification and why.

General **Babers**. The issue of principal concern to us is the fact that as the statutory dollar limitations on small purchases has been incrementally raised from $1,000 to $2,500 to $10,000 to the current $25,000 threshold, there has been no commensurate adjustment of any other statutory dollar thresholds. This precludes us from achieving the purpose of small purchases which is to provide a simplified method of making low dollar value purchases. The specific statutory provisions which should be considered for repeal or modification are listed in Appendix A of the Final Report on Simplification of Small Purchases prepared by Task Group No. 5 of the Executive Committee on Federal Procurement Reforms under Executive Order 12352 and in the letter to the Administrator, Office of Federal Procurement Policy (OFPP) reprinted from the *Federal Contracts Report* attached hereto. The reasons the listed statutory provisions should be considered for repeal or modification are discussed in Chapter 3 of the Task Group No. 5 report (also attached) and the letter to the Administrator, OFPP. We have annotated the excerpt from the Task Group No. 5 report to bring it up to date from its March 1984 date.

Final Report on Simplification of Small Purchases

[Prepared by Task Group No. 5; Approved for Distribution by the Executive Committee on Federal Procurement Reforms—March 1984]

CHAPTER 3—STATUTORY AND REGULATORY DOLLAR THRESHOLDS

This chapter discusses what is the single most important means of achieving what is sought in Section 1(e) of Executive Order 12352; that is, the simplification of small purchases. The statutory dollar limitation on small purchases for the Department of Defense is $25,000. The limitation for the Civil agencies remains at $10,000, although the Congrss has been requested to increase it to $25,000. (CICA raised to $25,000 1 Apr 85.) The Task Group could discern no reason for the statutory small purchase limitation not to be at a uniform level. A small purchase is a small purchase regardless of the organizational entity making the purchase. When the Office of Management and Budget made its request to the Congress on March 10, 1983, to raise the Civil agency limitation it was stated that "simplified procurement procedures for small purchases result in savings because of shortened procurement lead time and reduced paperwork." Also, simplification makes them more attractive to commercial suppliers with resultant increased competition and lower prices. These objectives have been recognized by the Congress since at least 1892 in the form of authority for negotiated procurement of low-dollar items. The rationale applies equally to both Defense and Civil agency small purchases. Some 18 million small purchase actions are made annually by Federal purchasing agencies. Civil agencies enter into one third of these actions. To deny the same benefits to the Civil agencies is contrary to the basic premise of Section 1(e) of Executive Order 12352.

As the basic small purchase limitation was raised incrementally by Congress over the years from $1,000 to $2,500 to $10,000, there has been no commensurate adjustment of many other statutory and regulatory dollar thresholds. When the most recent upward adjustment was enacted for the Department of Defense the long-standing thresholds of several other statutes were far exceeded. Many of these were exceeded for the first time. Unless there is upward adjustment, the much needed relief granted by the Congress to the Department of Defense is somewhat illusory. Civil agencies will find themselves in a similar circumstance if their small purchase threshold is raised. This statutory anomaly seems to exist because legislative drafters in the past did not couple increases in the statutory small purchase threshold to other related statutory requirements. The General Counsel of the Department of Defense addressed this problem in his February 24, 1982 letter to the Director, Office of Management and Budget proposing legislation to raise the current dollar thresholds of certain social and economic programs implemented through the contracting process. Also, it was proposed that a mechanism be provided to make future administrative adjustments to those thresholds in response to general inflationary trends without further legislative action. This Task Group strongly recommends this approach to a problem of long standing. For reference purposes this initiative is identified as Legislative Proposal DOD 97-135. As drafted its benefits would enure to the benefit of all Federal agencies making small purchases.

The Task Group examined another family of statutes in the course of its review and believes it deserves attention, either legislatively or administratively. These are the statutes with zero dollar thresholds which, or course, require their applicability to small purchases, as well as contracts of higher dollar value. The Task Group was reluctant to recommend these statutes for priority legislative attention because the record clearly shows that the small purchase process has survived in spite of their existence. This does not mean, however, that in a review, such as is being made by this Task Group, that they do not require examination. The question arises as to whether or not the recipient of each small purchase action should be required to research his each and every duty and responsibility under these statutes. Without questioning thir usefulness, if can be argued that some other means would serve the same end. As a general proposition, zero dollar threshold provisions should not be applicable to small purchases. The Task Group is of the opinion, however, that much could be accomplished by totally eliminating their applicability up to some higher threshold; for example, that for use of SF 44 (presently $2,500) or the competitive thereshold ($1,000 for DOD and $500 for the Civil agencies). A legislative initiative to this effect is recommended. In the alternative, if legislative action is not deemed advisable, it is recommended that an omnibus clause recogizing their existence be utilized to facilitate their incorporation by reference in small purchases rather than showing them in full text. A subset to this alternative would be the adoption of the DOD Master Solicitation Technique (see DAR 2-201(c) and DAR 3-501(e)) whereby the text of required clauses is prepositioned on a one-time basis with prospective suppliers and is incorporated into the purchasre order by reference to the Master Solicitation. A product elaborating on this procedure has been prepared for this report and is discussed in Chapter 6 as well as being appended with the other products of the Task Group.

The Task Group had recommended action on legislative proposal DOD 97-163 which was forwarded to the Director, Office of Management and Budget on October 14, 1982, by the General Counsel of the Department of Defense. This was considered to be a critical piece of legislation if Federal small purchases were to be truly simplified. It proposed, inter alia, raising the synopsis threshold for proposed procurements to $25,000. Absent this legislation, it was believed small purchases would become two-tiered, i.e., there would be a fairly well defined line of demarcation in terms of the complexity of small purchases at roughly the $10,000 level. The Task Group has taken cognizance of the enactment of P.L. 98-72 which establishes the synopsis threshold at $10,000 for all Federal agencies. This, in the opinion of the Task Group, will create both training and organizational problems in addition to frustrating efforts to expand automation of the small purchase process. The Task Group is sensitive to the interests of the small business community as regards the publicizing of proposed small purchases. It is believed, however, that these interests could have been better served by some alternative means without inhibiting the ability of purchasing organizations to react within hours or days to satisfy needs.

Small purchase regulatory guidance obviously is influenced to a great extent by statutory thresholds. The recommended statutory relief would set the tone which could open a floodgate of regulatory reform and simplfication. An attachment to the statutory and regulatory dollar thereholds product is a compilation of regulatory thresholds. If small purchases are to be truly simplified, these thresholds must be critically examined and raised wherever good business judgment indicates such revision. Procurement Executives, exercising the authority of their Agency Heads, need to aggressively pursue this effort within their respective organizations. They also should make an intensive review of agency policy and practices to identify any unilaterally imposed agency thresholds which are susceptible to upward revision.

In conclusion, and at the risk of redundancy, the Task Group must emphasize that the stated objective of Executive Order 12352 will never be realized in its fullest potential unless the recommendations in this Chapter are acted upon.

APPENDIX A

EXECUTIVE ORDER 12352 ON FEDERAL PROCUREMENT REFORMS IMPLEMENTATION GUIDANCE

STATUTORY AND REGULATORY DOLLAR THRESHOLDS

1. Purpose

In accordance with Section 1(e) of E.O. 12352, Task Group No. 5 was directed to: establish programs to simplify small purchases and minimize paperwork burdens imposed on the private sector, particularly small business, investigate Government purchase methods which are used or could be used by Government agencies; and identify methods which could be expanded in order to further simplify small purchase procedures, yet maintain the integrity of the Government.

2. Description of Module

A. *Objective and Scope*—The objective of this module is to make small purchases not only simpler and more cost effective but also to make them more attractive to commercial suppliers with the hope that there will be increased competition and lower prices as a result. This objective has been recognized by the Congress since at least 1892 in the form of authority for negotiated procurement of low-dollar items. Recently, the Congress in the Defense Authorization Act of 1982 again raised the small purchase dollar threshold from $10,000 to $25,000. Similar relief for the Civil Agencies was forwarded to the Congress on March 10, 1983, by the Office of Management and Budget. The forwarding letter stated that "simplified procurement procedures for small purchases result in savings because of shortened procurement lead time and reduced paperwork." This hypothesis is correct. The problem is that there has been no concomitant adjustment to other statutory thresholds impinging upon the procurement process. As the statutory small purchase limitation has moved upward over the years it has now far exceeded several of the other statutory thresholds. Unless these thresholds are adjusted to the same level as the small purchase threshold there will be basically two levels of small purchases, i.e., those heretofore considered small and those which are by definition small but have to comply with statutory requirements that are applicable equally to large purchases. The increase in the small purchase limitation will have been largely illusory as it pertains to this latter category. Two-tiered small purchases will exacerabate the problem of training small purchase buyers and will inevitably present organizational problems for some buying activities.

B. *Relationship to Other Modules*—This module is one of several related elements of the Task Group 5 effort. It impinges on all other modules.

C. *Importance to the Overall Goal of Implementing Subsection 1e*—Without statutory and regulatory dollar threshold relief the Federal agencies will be severely constrained in their attempts to simplify small purchase procedures.

3. Summary of guidance

Statutes with Various Dollar Thresholds—An agency survey was conducted in October 1982, both within the Department of Defense and amongst the Civil Agencies. A common cry heard throughout the small purchase community was the need to raise selected statutory thresholds that impinge on the procurement process. Many of those most frequently cited in the survey results are of long standing. It has been the failure over the years to adjust these thresholds upward to keep pace with the basic small purchase thresholds that now highlights the problem.

Based upon procurement data accumulated by the Federal Procurement Data Center for Fiscal Year 1982 there were 18 million small purchase actions made by Federal purchasing agencies. The aggregate dollars expended for small purchase actions in Fiscal Year 1982 totaled $12,076,314,000. The value of the average Federal small purchase action amounted to $659.00. As the data is collected for the increased Department of Defense small purchase threshold these numbers, particularly those relating to the number of small purchase actions, are expected to increase substantially.

Because of this volume of small purchase actions it is imperative that threshold relief be granted if the basic objective of Section 1(e) of E.O. 12352 is to be achieved. The Task Group recognizes that small purchases have been accomplished over the years with many zero dollar thresholds. A zero dollar threshold means that the particular clause, provision, or certification requirement is required of all purchases, regardless of dollar value. While relief in this area would be highly desirable in terms of the basic simplification objective it was believed that a more compelling case can be made in those cases where the statutory dollar threshold in a particular statute has been pegged and has remained static at that level. Therefore, the following have been identified for immediate relief:

Short title	U.S. Code citation	Present threshold
Examination of records by the Comptroller General	10 U.S.C. 2313(b)	(1)
Employment of the handicapped	29 U.S.C. 793(a)	$2,500
Affirmative Action disabled veterans and veterans of the Vietnam era.	38 U.S.C. 2012(a)	10,000
Davis-Bacon Act	40 U.S.C. 276(a)	2,000
Walsh-Healey Act	41 U.S.C. 35	10,000
Service Contract Act	41 U.S.C. 351(a)	2,500

Short title	U.S. Code citation	Present threshold
Solid Waste Disposal Act	42 U.S.C. 6962(a)	10,000
Small Business Act	15 U.S.C. 637(d)(2)(A) and (e)(1)(A)	10,000
Contract Work Hours and Safety Standards Act	40 U.S.C. 327-333	2,500
OFPP Act, as amended	41 U.S.C. 418(a)(1)(A), (2) and (3)	10,000

Ambiguous but susceptible to application to purchase orders which are contracts by definitions.

The foregoing statutory threshold changes were addressed by the General Counsel of the Department of Defense in his Legislative Proposal DOD 97-135 which was forwarded to the Director, Office of Management and Budget on February 24, 1982. Also contained in this legislative proposal was the recommendation that a mechanism be provided to make future administrative adjustments to those thresholds in response to general inflationary trends without further legislative action. This Task Group strongly recommends that this legislative initiative be moved forward to the Congress. As a means of further identification this proposed legislation, when enacted, was to be cited as the Social and Economic Program Adjustment Act of ——."

The Task Group wants the record the show that it does not oppose statutes that promote social and economic well-being through the contracting process. Take for example the three labor statutes in the foregoing list. Each was enacted to fulfill a perceived need for reform as it related to wages, hours of work, and working conditions. As the contracting process evolved every class of contract was covered, i.e., construction, supply, and ultimately service contracts. It is believed that these programs and others serving other needs have proven valuable over the years in achieving their stated goals. The Task Group is not questioning this aspect of these programs. What does come into question is the value of implementing them in the high volume, low dollar value small purchase program. Are these programs well served in this arena, bearing in mind the inflation that has transpired since their enactment? The Task Group believes the answer to be negative when the administrative costs and delays are weighed against the good to be achieved in a particular small purchase.

The Commission on Federal Paperwork has been quoted as follows: ". . . conditions or provisions incorporated in Government contracts to further social and economic objectives add many complicating factors to the procurement process. . . . To permit the threshold to remain unchanged is inconsistent with past practice and imposes a paperwork burden of considerable magnitude upon the Government and industry, particularly small business which does not command the resources available to larger firms and often cannot afford to hire additional clerical help, let alone maintain a staff of legal, fiscal, and accounting experts to provide advice on statutory and contractual requirements."

This quotation is particularly pertinent to the statutes enumerated above. It seems to apply also to the statutes discussed in the next part of this paper.

Statutes with Zero Dollar Thresholds—There is another family of statutes alluded to earlier that deserve attention, either legislatively or administratively. As defined earlier, these are the statutes with zero dollar thresholds which, of course, requires their applicability to all small purchases as well as contracts of higher dollar value. The Task Group was reluctant to recommend these statutes for priority legislative attention because the record clearly shows that the small purchase process has survived in spite of their existence. This does not mean, however, that in a review, such as is being made by this Task Group, that they do not deserve attention. The question arises as to whether or not the recipient of each small purchase action should be required to research his each and every duty and responsibility under these statutes. Without questioning their usefulness it can be argued that some other means would serve the same end. They are listed below:

Short title:	*U.S. Code citation*
Gratuities	10 U.S.C. 2207
Preferenece for U.S.-flag carriers	10 U.S.C. 2631
Officials not to benefit	18 U.S.C. 431
Convict Labor Act	18 U.S.C. 436
Copeland "Anti-Kickback" Act	18 U.S.C. 874
Conservation of energy	42 U.S.C. 6361
Preference for U.S.-flag air carriers	49 U.S.C. 1517

In the opinion of Task Group 5 this group of zero threshold provisions should not be applicable to small purchases. A legislative initiative to this effect is strongly recommended. In the alternative, if legislative action is not deemed advisable, it is recommended that an omnibus clause recognizing their existence be utilized to facilitate their incorporation by reference in small purchases rather than showing them in full text. A subset to this alternative would be the adoption of the DOD Master Solicitation Technique (see DAR 2-201(c) and DAR 3-501(e)) whereby the text of required clauses is prepositioned on a one time basis with prospective suppliers and is incorporated into the purchase order by reference to the Master Solicitation.

Synopsis and Other Provisions of the Small Business Act—Task Group 5 had singled out for special treatment the synopsis requirement and related statutory provisions of the Small Business Act which were addressed by the General Counsel of the Department of Defense in his legislative proposal, DOD 97-163, which was forwarded to the Director, Office of Management and Budget on October 14, 1982.

The Task Group was particularly concerned with the synopsis requirement. Of all the statutory thresholds in need of upward revision from a buying operations standpoint, the requirement for synopsis of proposed procurements in the Commerce Business Daily was perhaps the most critical. From the date of its enactment it was never contemplated that it would apply to small purchases. Unless it were revised upward to $25,000 small purchases would operate on a two-tier basis. Because of the synopsis requirement those agencies which already had sophisticated systems for automation of small purchases would be unable to use such systems effectively without substantial reprogramming.

The synopsis requirement has now been made more rigorous by the enactment of P.L. 98-72. This alone will, to a large degree, defeat any benefit to be derived from the raise in the basic statutory small purchase threshold. This is an issue of vital concern to the entire Federal procurement community. What should have been weighed were the possible alternatives of synopsis and increased competition against the need for small purchase procedures which could react within hours or days to satisfy needs. The Task Group believes the historic intent of statutory authority to make small purchases in the manner common among businessmen argued in favor of the latter alternative. A reexamination would appear to be in order.

Regulatory Dollar Thresholds—Task Group 5 compiled 30 pages of regulatory thresholds which should serve as a valuable guide for possible threshold raising action. Each threshold is briefly described and the pertinent DAR, FPR or FPMR, and FAR citation are given. While the Task Group notes that in many instances the regulatory coverage has been driven by a statutory threshold other instances exist where the dollar level appears to have been established solely through the regulatory process. The latter should receive immediate attention. In some cases there is no explicable rationale for disparate threshold levels between DAR, FPR, and FAR. Immediate action is indicated in these cases to raise the threshold to the highest level. Since the thresholds compilation was made the Department of Defense has raised several of its regulatory thresholds and published the changes to DAR in DAC 76-40.

In particular, the elevation of the competition level from $500 to $1,000 within the Department of Defense is applauded by the Task Group. Based upon the survey of Civil Agencies similar action should be taken immediately to revise the FPR and FAR. Similarly, the DAR has been revised to raise the threshold for employment of the Fast Payment procedure to $25,000. Lack of counterpart FPR coverage is noted and should be corrected. A separate Task Group 5 Product will examine the Fast Payment procedure in depth. Many other aspects of the mechanics of making and paying for small purchases are the subject of discrete Task Group 5 Products. Review of the attached regulatory threshold compilation with the objective of early revision upward of those which are not driven by statute is strongly recommended. Also, Procurement Executives should review their respective agency policies and practices to identify any agency imposed thresholds under $25,000 which are susceptible to upward revision.

4. Enumeration of actions needed to implement the guidance

A. Actions that can be taken by agency heads without any change in law or the FAR/DAR/FPR. Review of agency policy and practices to identify any agency imposed thresholds under $25,000 which should be re-examined for possible upward revision.

B. Actions whose execution depends on changes to FAR/DAR/FPR or other governing regulations or policy documents. Those contained in Attachment 1 entitled Thresholds.

C. Actions whose execution depends on changes in statutes. Those contained in Attachment 2 and 3.

5. Date of completion of module, September 30, 1983.

TEST PROGRAMS BEING CONSIDERED BY OFPP REGARDING SIMPLIFIED SMALL PURCHASE PROCEDURES, AUTOMATED PROCUREMENT ORDERS, AND EXCISE TAX EXEMPTION FOR MILITARY VEHICLES

Honorable Donald E. Sowle
Administrator
Office of Federal Procurement Policy
Office of Management and Budget
Washington, DC 20503

Dear Mr. Sowle:

Enclosed for your consideration is a test plan developed jointly by the General Services Administration (GSA), the Department of Defense (DOD) and the National Aeronautics and Space Administration (NASA) for conducting simplified small purchases. This proposal is submitted under the authority of Public Law 98-191, which authorizes the OFPP to conduct Government-wide studies of ways to improve the Government procurement process. This proposal is designed to make timely and economic acquisitions of low dollar value purchases as originally intended by Congress, primarily by consistently applying existing small purchase thresholds now in legislation. We intend to reserve small purchases for small businesses on a test basis.

This initiative is consistent with recommendations made in the Final Report on Simplification of Small Purchases by Task Group 5 of the Executive Committee for Federal Procurement Reform. Also, the President's Private Sector Survey on Cost Control estimated almost $200 million annual savings if the socio-economic thresholds were consistently applied at the small purchase level. Our goal is to obtain these savings as early as possible. On this basis, DOD will again include in its legislative initiatives a proposal to raise the statutory thresholds.

Consistent with this DOD initiative, our proposal envisions conducting the small purchase test within GSA, DOD and NASA. We believe the authority for the test should be structured so that OFPP could designate additional agencies for participation in the test.

We understand that your office feels that authority other than that contained in Public Law 98-191 is required to conduct this test. Your office will need to address how these statutory waivers should be obtained. If you determine legislation is necessary, we have attached draft legislation for your consideration.

We consider raising these statutory thresholds consistent with Congressional intent and that the improved efficiencies and economies are self-evident. Nonetheless, our agencies remain strongly committed to obtaining this test authority to further substantiate our position and we will work with you in that regard.

Sincerely,

ALLAN W. BERES
Assistant Administrator
for Acquisition Policy
General Services
Administration

MARY ANN GILLEECE
Deputy Under Secretary
for Acquisition Management
Department of Defense

S. J. EVANS
Assistant Administrator
for Procurement
National Aeronautics
and Space Administration

Enclosures

INNOVATIVE PROCUREMENT METHODS

I. Title: Test Simplified Procurement Practices for Small Purchases.

II. Statement of Need and Objectives: Ensure that the Government has a fast, easy to understand, and inexpensive procedure for low dollar purchases, by eliminating numerous unnecessary provisions from small purchases and returning this category of procurement to the level of efficiency originally intended.

When the Armed Services Procurement Act of 1947 and the Federal Property and Administrative Services Act of 1949 (Acts) were enacted, they provided for the use of small purchase procedures for purchases up to $1,000. These small purchase procedures were authorized to provide for the efficient and inexpensive procurement of relatively small dollar value items and services. Over the years, the Acts have been amended to raise the small purchase threshold, first to $2,500, then to $10,000, and in 1981 and 1983, to the current threshold of $25,000. The adjustments to the threshold reflected Congress' recognition of the impact of inflation on what constitutes a low dollar value purchase.

Over the years, Congress also enacted a variety of legislation, generally outside of the major procurement statutes, which nonetheless have imposed significant requirements on the contracting process. At the time of their enactment, Congress usually recognized the need to balance the benefits of the legislation (often unrelated to the commercial transaction) with the potential adverse impact of its requirements on the economy and efficiency of the procurement process. As a result, the statutes were frequently drafted so as to have little or no application to small purchases. This was accomplished by setting the "floor," in terms of contract dollar value, for the statute's applicability at the existing statutory "ceiling" for use of the small purchase authority.

Unfortunately, although the "ceiling" for small purchasing has been regularly adjusted to take into account the declining purchasing power of the dollar, the "floors" for applying other statutory requirements have not always kept pace. As a result, and contrary to the original intent of Congress, the requirements of these statutes have become applicable to many small purchases. Thus, procedures originally intended to ensure the expeditious and economic acquisition of low dollar value items and services are now subject to a wide array of relatively complex and costly administrative steps, solicitation provisions, and contract clauses. The resultant burdens are felt not only by the Government, but also by the private sector, particularly small businesses.

The rationale for the test is to verify the hypothesis that the use of unencumbered, simplified small purchase procedures could accomplish the following:

1. Reduce procurement costs.
2. Alleviate paperwork burdens on Government and industry vendors.
3. Reduce procurement leadtime.
4. Increase small business participation.
5. Provide for efficient and inexpensive procurements without adversely affecting beneficiaries of other statutory provisions.

III. Proposed innovative procurement method. All statutory and regulatory provisions currently applicable to small purchases which are impeding the efficient and inexpensive procurement of small dollar value (under $25,000) items and services will be eliminated. For test purposes, all purchases under $25,000 will be reserved for small business under small business - small purchase set-asides unless the contracting officer determines that he/she cannot reasonably expect to obtain two or more offers from small business concerns that will be competitive in terms of market price, quality, and delivery.

IV. Applicable policy objectives from P.L. 98-191. The proposed innovative procurement methods are consistent with the following policies contained in the Office of Federal Procurement Policy Act:

1. Promoting full and open competition;
2. Establishing policies, procedures, and practices which will provide the Government with property and services of the requisite quality, within the time needed, at the lowest reasonable cost;
3. Promoting the development of simplified uniform procurement processes;
4. Promoting the participation of small business concerns;
5. Supporting the continuing development of a competent, professional work force;
6. Eliminating fraud and waste in the procurement process;
7. Eliminating redundant administrative requirements placed on contractor and Federal procurement officials;
8. Promoting fair dealings and equitable relationships with the private sector;
9. Ensuring that payment is made in a timely manner and only for value received;
10. Requiring, to the extent practicable, the use of commercial products to meet the Government's needs;

V. Criteria for determining the success of the test program.

A. Reduce procurement costs. We will compare prices paid for the same or similar items or services procured using the existing small purchase procedures with purchases made using the test procedures. The test will be considered successful if the test procedures consistently produce significantly lower prices.

B. Alleviate paperwork burdens on Government and industry. We will compare the paperwork burden placed on the Government and industry under the current procedure vs the test procedure. Success will constitute (1) a reduction in burden without a detrimental effect on the quality of the item or service and (2) an increase in the number of vendors who are interested in competing for contracts.

C. Reduce procurement leadtime. We will compare the procurement leadtime for the same or similar items or services procured using the existing small purchase procedures with purchases made using the test procedures. The test will be considered successful if the test procedures consistently produce significantly shorter procurement leadtimes.

D. Increase small business participation. We will compare the number of small businesses who are interested in competing for work under the

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Published by THE BUREAU OF NATIONAL AFFAIRS, INC., Washington, D.C. 20037

current procedures vs the test procedures. The test will be successful if more small businesses are found to be competing for work under the test procedures.

E. Provide efficient and inexpensive procurements without adversely affecting beneficiaries of other statutory provisions. The effects of the test procedures on the beneficiaries of other statutes, will be examined, whenever measurable, and the test will be successful if there is no adverse impact on the intended beneficiaries, inconsistent with the statutory objectives.

VI. Measurement Plan and Schedule.

A. Overall Plan and Schedule. The General Services Administration (GSA), the Department of Defense (DOD) and the National Aeronautics and Space Administration (NASA) will coordinate the conduct of the test. It is anticipated that the test authority would be available for up to a 2-year period. A coordinating group composed of representatives of the two agencies shall devise procedures to ensure the validity of the test results. Separate test steering groups, within GSA, DOD and NASA shall develop test training plans and ensure that participating offices selected as test sites are properly prepared. The performance of the test activities will be monitored by the agency steering groups. Continued coordination between GSA, DOD and NASA will take place during the test period.

The Federal Acquisition Institute (FAI) will assist in developing questionnaires to determine the test results and in performing analyses to determine test validity.

B. Items to be Measured. Items to be measured shall consist of relatively standard commercial items and services which are easily measurable and for which decentralized purchasing is feasible. Examples: (1) painting cost/sq. ft., (2) cleaning cost/sq. ft., and (3) standardized commercial supplies (plumbing, electrical, office supplies, etc.). Standard quality control procedures and reporting would be used to determine that the item or service acquired under the test procedures was similar to the items received in the past or by the control group.

1. Reduction in Prices. We will determine reduction in prices by comparing prices paid by the test group with:

a. Historical prices paid for items or services in like or similar quantities during the past year(s) after adjustment for inflation.

b. Prices for the same or similar items/services by other procurement offices using current procedures (the control groups).

2. Alleviate paperwork burden.

a. In previous submittals to OMB related to the Paperwork Reduction Act, we have established standard burden hours for many of the reporting procedures resulting from the Public Laws cited in Section VII, Applicable Statutes. We will use this formula to calculate the savings to the public and the Government by eliminating the reporting requirement of these statutes.

b. We will also use the items to be measured in item #B above (i.e. painting cost/sq. ft.) and calculate any change in the numbers of bidders between the test group and (1) historical records of bidders for the items or services in like or similar quantities during the past year(s) and (2) the control group.

3. Reduce procurement leadtime.

a. Measure the time from receipt of the requirement by the procuring official to the date of award.

b. Measure the response time from issuance of the request for quotations/proposals to the date for submission of quotations/proposal.

c. Paperwork burden placed on the commercial organization and its contractors in obtaining supplies or services in like or similar quantities to the test group.

4. Increase small business participation. The extent of any increased small business participation in the procurement process will be evaluated by comparing small business participation between (1) the test group and historical data and (2) the test group and the control group.

VII. Applicable statutes, regulations, or procedures to be waived or changed.

Legislation would be required to raise the threshold for application of statutes, Executive Orders, and administrative regulations to $25,000 to coincide with the dollar ceiling established for small purchase procedures. The legislation would, in effect, state that: Notwithstanding any other provision of law, simplified procedures may be established to economically and efficiently make small purchases.

Existing statutory requirements for which waiver is requested:

1. Service Contract Act (41 U.S.C. 351(a).
2. Davis-Bacon Act (40 U.S.C. 276(a).
3. Small Business Act (15 U.S.C. 637(d)(2)(A) and (e)(1)(A).
4. Walsh-Healey Act (41 U.S.C. 35).
5. Contract Work Hours and Safety Standards Act (40 U.S.C. 327-333).
6. Rehabilitation Act of 1973 (29 U.S.C. 793(a).
7. Vietnam Era Veteran's Readjustment Assistance Act (38 U.S.C. 2012(a)).
8. OFPP Act, as amended (41 U.S.C. 418(a)(1)(A).

Other requirements for which waiver is requested:

1. Equal Employment Opportunity provisions.
2. Reporting requirements of OMB Circular A-40.

VII. Scope of test.

We plan to conduct the test procedures in selected DOD, GSA and NASA field offices which procure supplies, services and construction.

Offices selected will procure a variety of items which are similar so comparisons can be easily made. Also purchases are expected to be of a repetitive nature so past purchases in the same office as well as purchases being made at the same time in other offices can be compared.

A group of offices would be identified as a control group and another group identified as the test group. DOD, GSA and NASA will establish the number of purchases that need to be reviewed to provide a valid sampling of the test results.

A BILL

TO AUTHORIZE THE TESTING OF SIMPLIFIED PROCUREMENT PRACTICES FOR SMALL PURCHASES

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled.

Section 1. (a) The Office of Federal Procurement Policy Act Amendments of 1983, Public Law 98-191, authorized the Administrator for Federal

Procurement Policy to test innovative procurement methods and procedures consistent with the policy objectives set forth therein, and (b) the Administrator has recommended that a test be authorized for the use of simplified procurement practices in small purchases, which, heretofore, could not be conducted due to statutory constraints.

Section 2. At the time of enactment, the statutes identified herein for waiver were made inapplicable to small purchases in order to facilitate the economic and efficient purchase of relatively small dollar value items and services. However, with the ceiling for small purchasing having been regularly adjusted to take into account changing economic conditions and and with the floor for applying other statutory requirements not having been similarly adjusted, the unintended effect is that these statutes have become applicable to small purchases with potential impact on the economy and efficiency of the procurement process. The test shall determine the identifiable impact of raising the statutory thresholds to a level consistent with the small purchase threshold on the economy and efficiency of the procurement process while considering the impact on the private sector.

Section 3. Accordingly, the General Services Administration, the Department of Defense and the National Aeronautics and Space Administration are authorized consistent with the requirements of Section 15 of Public Law 98-191, to conduct a test of simplified procurement practices for small purchases, and shall report to Congress through the Office of Federal Procurement Policy as to their findings.

Section 4. For the purposes of conducting this test, all purchases under $25,000 will be reserved for small business under small business - small purchase set asides unless the Government determines that it cannot reasonably expect offers from two or more small business concerns that will be competitive in terms of market price, quality and delivery.

Section 5. For the purposes of conducting this test, the following statutes are amended for a two-year period from inception of the test:

a. Section 2313(b) of Title 10, United States Code, is amended by inserting "in excess of $25,000" after "under this chapter."

b. Section 8(d)(2)(A) of the Small Business Act (Public Law 95-507; 92 Stat. 1767; 15 U.S.C. 637(d)(2)(A)) is amended by striking out "$10,000" and inserting in lieu thereof "$25,000."

c. Section 8(e) of the Small Business Act (Public Law 98-72; 15 U.S.C. 637(e)(1)(A) is amended by striking out "$10,000" and inserting in lieu thereof "$25,000."

d. Section 503(a) of Public Law 93-112 (87 Stat. 393; 29 U.S.C. 793(a)) is amended by striking out "$2,500" both places it appears and on each occasion inserting in lieu thereof "$25,000."

e. Section 2012(a) of title 38, United States Code, is amended by striking out "the amount of $10,000 or more" in the first sentence and inserting in lieu thereof "in excess of $25,000."

f. Section 1(a) of the Act of March 3, 1931, ch. 411, 46 Stat. 1494, (40 U.S.C. 276(a)), is amended by striking out "$2,000" and inserting in lieu thereof "$25,000."

g. Section 329(a) of Title 40, United States Code is amended by inserting "in excess of $25,000" after "to any contract."

h. Section 418(a)(1)(A) of the OFPP Act (Public Law 98-191; 41 U.S.C. 401), as amended, is amended by striking out "$10,000 and inserting in lieu thereof "$25,000."

i. Section 1 of the Act of June 30, 1936, ch. 881, 49 Stat. 2036 (41 U.S.C. 35), is amended by striking out "$2,500" and inserting in lieu thereof "$25,000."

j. Section 2(a) of the Service Contract Act of 1965 (Public Law 89-286; 79 Stat. 1034; 41 U.S.C. 351(a)), is amended by striking out "$2,500" and inserting in lieu thereof "$25,000."

OFFICE OF THE UNDER SECRETARY OF DEFENSE
WASHINGTON DC 20301 -3060

RESEARCH AND
ENGINEERING
(AM)

Honorable Donald E. Sowle
Administrator
Office of Federal Procurement Policy
Office of Management and Budget
Washington, D.C. 20503

Dear Mr. Sowle:

Attached for your consideration are two test plans for innovative procurement methods (Enclosure 1). These tests are in addition to our participation in the test now being developed by the General Services Administration on the waiver of certain socioeconomic procurement provisions for small purchases at selected test activities (Enclosure 2).

Your representative may call Mr. Wayne Wittig (697-8334) of my office if any additional information is required. Please keep us informed of the progress of these test plans.

Sincerely,

MARY ANN GILLEECE
DEPUTY UNDER SECRETARY
(ACQUISITION MANAGEMENT)

Enclosures

I. Title of test program.

Paperless Procurement System

II. Brief Statement of Need and Objectives:

There is a need to eliminate internal hard copy documentation (delivery orders and purchase orders) as the basis for contract administration and payment and move into a fully automated method of contracting. Implementation costs cannot be precisely quantified as of this date. Substantial system capability to provide for mechanized storage of transmitted orders and on line interrogation would be required. These developmental costs, however, should be offset by substantial benefits in reduced administrative storage and retrieval costs, printing costs, etc.

2-4-85

Published by THE BUREAU OF NATIONAL AFFAIRS, INC., Washington, D.C. 20037

III. Proposed Innovative Procurement Methods:

Defense General Supply Center (DGSC), a field activity of the Defense Logistics Agency, has developed an automated system which enables it to transmit orders negotiated indefinite delivery type contracts with these contractors. When a requisition is received for one of the items on the contracts, it is processed through a series of system screening criteria to determine eligibility for the automated order placement system. If the item, quantity, dollar value and customer location are within the terms of the contract, the requirement is passed directly by machine transmission to the contractor. Within hours after receipt of the order from DGSC the contractor taps its commercial distribution system to deliver the material directly to our military customer from its closest distribution point. The items on contract are standard commercial items and may be shipped from stock on hand in periods as short as three to six days.

The machine to machine transmission of orders externally was the first developmental step. The goal is to further automate the process by eliminating internal hard copy orders in the system data base and provide a means for on line interrogation prior to making any necessary order modifications and payment.

Although we would propose testing of this concept in conjunction with the automated order placement system at DGSC as a demonstration project, the potential exists for expansion of the concept ultimately to most if not all small purchase transactions.

IV. Applicable Policy Objectives from P.L. 98-191:

This test promotes the objectives of the Office of Federal Procurement Policy Act by eliminating redundant administrative requirements, reducing administrative costs associated with acquiring Government property and ensuring timely payment.

V. Criteria for Determing the Success of the Test Program:

The following will be measured:

1. Savings in printing costs
2. Savings in contract file storage and retrieval
3. Savings in administrative processing costs

The project will be considered successful if savings outweigh developmental and implementation costs.

VI. Measurement Plans and Schedule:

After approval of the conceptual test plan, a more definitive plan will be developed which lays out a reasonable schedule for the extensive programming changes which are required.

VII. Applicable Statutes, Regulations, or Procedures to be Waived or Changed:

31 U.S.C. 1501 - This is the only statute apparently requiring valid government requirements to be recorded in writing.

Federal Managers' Financial Integrity Act of 1982 - Addresses the establishment and enforcement of accounting controls to safeguard assets including verifying the proprietary and accuracy of transactions and clearly defining an audit trail.

General Accounting Office Manual for Guidance for Federal Agencies, Section 18.2, requires that disbursements be supported with basic payment documents, i.e., contracts and purchases orders.

ASPR Supplement No. 2 -- Contract File, Maintenance, Closeout, and Disposition (ASPS No. 2) (1 Apr 70)

VIII. Scope of Test

All automated order placement contracts at DGSC would be included in the test. There are currently two contracts which have had approximately 20,000 orders placed against them to date since their inception in April 1983. The DGSC point of contact is Ms. Barbara Dance, (804)-275-3431.

Appendix A - Suggested Statutory and Regulatory Changes:

1. The two identified statutes should be amended as follows:

The requirement for supporting documentary evidence may be met through design of an auditable automated system in lieu of the hard copy form of recording each single transaction.

2. A deviation to the ASPR Supplement 2 should be processed to eliminate the requirement for maintenance of contract files for purchase orders. (Note: Federal Acquisition Regulation Part 4 of Contract File Retention is optional for small purchases.)

I. Title of Test Program:

DoD Exemption of Federal Excise Tax (FET) on Military Vehicles.

II. Brief Statement of Need and Objectives:

Procurements involving FET cause nonproductive workload problems both to the Army's Tank and Automotive Command (TACOM) and its contractors. The law requires payment of FET by the manufacturer for all road vehicles over 33,000 pounds used domestically unless a private tax ruling by the Internal Revenue Service applies. The manufacturer passes on the amount of the FET to the buyer. When the buyer is the government, it is just taking money from one pocket to put in another while causing a large administration burden. FET applicability is vague on some military vehicles. A determination must often be made of the vehicle configuration and use for purposes of applying the FET as well as obtaining a legal opinion on applying any private rulings by the Internal Revenue Service. Solicitations have been released when FET application was in doubt where no clear decision on its application was available to the buyer. These contracts have, on occasion, ended in litigation covering FET application.

Also, on FET applicable contracts, when the destinations change from overseas to stateside or vice versa, the vehicle price has to be renegotiated with the contractor. This is a time consuming process that takes at least six weeks to resolve. Without FET applying, the action would be a simple destination change that would take less than a week to accomplish. Eliminating FET on DoD military vehicles would avoid unnecessary funds transfers within the government, simplify the procurement process, greatly reduce nonproductive workload problems, and save time and money on government solicitations by reducing administrative lead time and litigation afterwards.

III. Proposed Innovative Procurement Methods:

FET is currently applicable on select vehicles. For the test, some of these vehicles will be solicited with FET not applicable to determine if the Government can reduce nonproductive workload problems and reduce FET based litigations.

IV. Applicable Policy Objectives from P.L. 98-191:

This test would help establish policies, procedures, and practices which will provide the Government with property and services of the requisite quality, within the time needed, at the lowest reasonable price.

The test will also help promote the development of simplified uniform procurement processes.

V. Criteria for Determining the Success of the Test Program:

The success of the test program will be determined by the time saved during the life of the contract. The main savings will be from contract modifications dealing with destination changes. A slight time change will occur from getting procurements on the street faster.

Success will be determined by any significant reduction in the nonproductive workload problems encountered by the buyer. Reducing time spent modifying destination changes from six weeks to one and quicker procurement actions are significant reductions.

The time saved by eliminating a cause of litigations unfortunately cannot be tested. This is due to not knowing which contracts will end up in litigation.

The faster a procurement can be made and the fewer contract administration problems a contract specialist encounters during the life of a contract, ensures the Government getting required vehicles on time and at a reasonable price. This will also enable the contract specialist to devote more productive time to his/her work in general.

VI. Measurement Plans and Schedule:

Upon approval of eliminating FET on test items, selected contract specialists will procure under both conditions. The contract specialists will keep track of all actions and time involving FET, e.g., processing time of a D&F to legal to determine FET applicability, processing modifications involving destination changes from overseas to stateside or vice versa.

VII. Applicable Statutes, Regulations or Procedures to be Waived or Changed:

The applicable statute to be waived or changed is the Highway Revenue Act of 1982, Title V (Public Law 97-424 dated January 6, 1983).

VIII. Scope of Test:

The test plan will compare the problems of FET required vehicles versus vehicles of the same class with FET being applicable. The test will run the length of the contracts.

A minimum of four vehicles will be selected for the test. The vehicles will be chosen upon test approval on FET applicable items just entering the procurement process.

The only agency that is to be involved in the test is TACOM. The Special Truck Section, AMSTA-ISAA, has been selected to do the test program's procurement.

Point of Contact at TACOM is Mr. G. P. O'Brien, AUTOVON 786-8144.

Appendix

The Highway Revenue Act of 1982, Title V (Public Law 97-424 dated January 6, 1983) will need to be amended to exclude vehicles purchased for military use.

QUESTIONS SUBMITTED BY SENATOR CARL LEVIN

SPECIAL JOINT LOGISTICS COMMANDERS COMMITTEE ON TECHNICAL DATA

Senator LEVIN. Admiral Hughes, it is my understanding that the Joint Logistics Commanders have a special committee on data rights. What issues does this committee review? Has this Committee yet, or will it in the future, recommend any policy for implementation by one or more of the services?

If so, how will the results of this special committee's work be integrated with the DAR Council regulatory process and the opportunity for public notice?

Admiral HUGHES. The Joint Logistics Commanders established a special panel on "Government Data Rights" to better assure the availability of technical data packages needed for competitive reprocurement of equipment and spare parts. To be usable, these packages must be unencumbered by inappropriate restrictive markings.

This panel was charged with establishing improved procedures for protecting government rights in technical data and computer software pertaining to items, components and processes developed with government funding. The panel is now identifying deficiencies in existing procedures for possible improvements. The Joint Logistics Commanders anticipate issuing uniform procedures for better protecting the Government's rights during 1986. These procedures are planned to be consistent with the Federal Acquisition Regulation; therefore changes in law or regulation would not appear to be necessary to accomplish the results we seek.

GENERAL AND ADMINISTRATIVE EXPENSES INCLUDED IN PROFIT CALCULATIONS

Senator LEVIN. During our Acquisition Policy Subcommittee hearings earlier this year, I questioned DOD officials and defense contractors about the current Department of Defense markup policy. Under your rules, you permit defense contractors to earn a "profit" based in part on the size of the contractor's general and administrative expense. In my judgment, this offers the contractor an incentive to increase costs.

I offered an amendment which has been included in the fiscal year 1986 DOD Conference report (section 903) which asks for a report by the Secretary of Defense on the desirability of continuing the current policy.

Since that time, the Department's DFAIR study has been released. In that study, the DFAIR team noted: "An argument can be made for excluding G&A from the markup base. If excluded, any incentive provided by the markup policy for a contractor to increase G&A costs would be removed."

Could you support a change in DOD policy which excludes G&A from the markup base for your service?

If you agreed with such a change, would such an action require legislation or could it be done administratively?

General SKANTZE. We have long recognized that along with its advantages, DOD profit policies have some built-in disadvantages. The point you raise on G&A is one of those disadvantages. The higher the contractor's G&A expense is, the larger the cost base becomes which is used to calculate the Government's negotiation goal for profit. Unfortunately, this principle applies not only to G&A but also to all other costs as well. The Defense Financial and Investment Review (DFAIR) Study was conducted in part to develop methods to defeat this built-in problem that is present in a cost based profit system.

We are not opposed to removing G&A from the profit application base as long as it is done in a coordinated fashion with other changes to DOD profit policies so that a cohesive, effective and fair profit policy results.

A change such as this does not require legislation. It is within the authority of the DOD to issue.

NAVY RESPONSE. The argument for excluding G&A from the markup base primarily rests on three propositions: (1) contractor markups are too high: (2) the emphasis of cost on contractor markups should be reduced: and (3) G&A expenses are at the top of the list of costs that should be controlled. The Navy concurs in these propositions and favors eliminating G&A from the markup base. To the extent that differing G&A rates are caused by the inclusion or exclusion of similar costs in contractor accounting systems, inequities may result unless care is taken in defining G&A.

This action could be taken administratively. It would require a revision to the FAR, but not require any legislative action.

AGENCY PURCHASING OFFICERS' MORALE

Senator **Levin**. In a recent interview, one of the OSD acquisition deputies stated that the morale of the acquisition work force had "sunk so low they don't talk to their relatives about it."

General **Skantze**. Yes, there is a morale problem in the contracting work force.

Senator **Levin**. Do you share that view of the morale of the Department's and your service's acquisition work force?

General **Skantze**. The continuous horror stories and criticism from the public, coupled with increasing workloads, have contributed to this decline in morale. However, we have established several initiatives to help keep our people motivated. We have established two new awards to recognize careerists who excel in the field. The "Outstanding Contribution to Increased Competition Award" was established and first presented in 1983 to personnel who enhanced the competitive process. Another new award, "The Air Force Professional in Contracting Award," was established and presentations were made to the first recipients in August 1985 by Secretary Verne Orr. This award recognized demonstrated dedication and professionalism on the part of contracting personnel and emphasizes the Air Force's high level of interest in enhancing professionalism. While these efforts are relatively new, the reception by the work force has been positive.

Senator **Levin**. Don't events such as the Navy Secretary's preciptious action to fire the three officials at the Miramar Naval Air Station contribute to the work force's fear of either making a mistake or overpaying for some parts?

General **Skantze**. This question cannot be answered by the Air Force.

Senator **Levin**. What actions has your service taken to enhance the professionalism of the work force.

General **Skantze**. The Air Force has taken specific actions to enhance professionalism of the work force. Training, education and rewards have become major focal points in our management of personnel resources. Our "COPPER TOP" program, for example, examines current training shortfalls within the contracting work force. One of the program's major successes to date has been approval of extra funding in the fiscal year 1987/89 Program Objective Memorandum to correct a 60 percent shortfall of completion of mandatory training courses. Our centrally-managed and funded competitive intern program, "PALACE ACQUIRE" is targeted to recruit recent quality college graduates to entry-level trainee positions in a variety of occupational fields. This program helps to maintain civilian work force stability and expertise in major functional areas by providing a pipeline of available and highly skilled civilian employees. The eventual success of these initiatives in contributing to the accomplishment of the desired objectives of enhancing professionalism and raising the morale of the contracting work force will require the support of not only those who are responsible for the execution of the programs, but also of the Congress to ensure that the necessary funding continues to remain available for this effort.

Navy Response. Navy Department contracting personnel are highly motivated and dedicated to supporting operational fleet requirements. We agree that our personnel are sensitive to the public criticisms of the problems in the contracting process which have been highlighted and singled out on a wide and continuing basis. With the unprecedented amount of legislative reform which has been implemented within the past few years, we need training and time to fully implement these reforms.

The Secretary of the Navy temporarily relieved three officers at the Miramar Naval Air Station because he had lost confidence in their ability to perform their duties. Two of the three officers were eventually reinstated. This is a prerogative of a senior in the military chain of command.

In the area of actions taken to enhance the professionalism of the work force, the Navy took the lead by assuming the leadership of Task Group Six. This Group was chartered by the Federal Committee on Federal Procurement Reform to develop guidance on establishing procurement career management programs under Executive Order 12352.

The Navy played a key role in a comprehensive review of training, education and experience prerequisites for military and civilian acquisition personnel directed by DEPSECDEF.

The Navy has taken a step toward creating a corps or cadre of educated, skilled acquisition professionals with the establishment of the Material Professional (MP) program for Naval officers engaged in acquisition and logistics. While it is too early to see the results of the MP program, all signs indicate that it will work. The program provides the basics, education and experience, and assures motivation through allocation of flag officer billets to members of the MP program.

PENALTIES FOR CONTRACTORS

Senator LEVIN. Included in the 1986 DOD conference bill are a number of significant penalties that will be imposed on defense contractors for submitting false claims, and overcharging for work, for example.

1. Do you believe these penalties will act as an effective deterrent to fraud for contractors doing business with the Pentagon?

2. Should these penalties be applicable to any contractor doing business with the *Federal* government, not just DOD?

3. Are these sanctions enough of a deterrent for DOD contractors?

General SKANTZE. 1. Yes. We believe the penalties will act as an effective deterrent to fraud.

2. Yes. The penalties should apply to all Government contractors.

3. Yes. The sanctions are a sufficient deterrent for DOD contractors.

NAVY RESPONSE. The Navy endorses the penalties set forth in sections 931, 932 and 934 of the Department of Defense Authorization Act, 1986, as reasonable, desirable, and necessary. The criminal fines and civil penalties should be of a magnitude that will effectively deter wrongdoing by Government contractors. Further, these prohibitions and penalties should also be applicable to all contractors doing business with the Federal Government.

COMPETITION

Senator LEVIN. One of the goals of the 1984 legislation was to open up the Federal procurement process to new players, particularly small and minority business.

Have you seen an increase in the number of new competitors for many of your service's purchases?

General SKANTZE. Yes we have. The increases became even more obvious after the Air Force established its Competition Advocate Program in January 1982. Since that time, the momentum for increased competition has grown significantly and is continuing to grow. The Air Force competed more than 82% of its 3.4 million procurement actions in fiscal year 1985, an increase in some 140,000 competed actions over fiscal year 1984. Other data, primarily having to do with small business, shows that we received over 7,300 requests from vendors wishing to be approved as qualified sources. Approximately 60% of these were approved, with 23% still under review at year's end.

Senator LEVIN. Is your service getting a better deal for its dollar because of this new competition?

General SKANTZE. The Air Force well recognizes the cost, performance, schedule, quality, and other benefits that can be obtained from competition. A good example of the benefits of competition is the engines for the F-15 and F-16 fighter aircraft. The Air Force developed an acquisition strategy requiring both Pratt & Whitney and General Electric to provide fighter engine candidates with product warranties and data rights. Both companies responded with engines having greatly improved operability, reliability, and warranty provisions as well as continued competition in the procurement. The result is two engine suppliers and an estimated life cycle cost avoidance of $525 million cost savings for spares procurements resulting from competition, breakout, price challenges and more economical buys. The fiscal year 1985 estimate, based on nine months of data, should exceed $500 million. The DOD report to Congress on Compeititon will include other "good news" examples.

Senator LEVIN. As part of the 1984 legislation, Congress formally established the Competition Advocate program. How successful are the competition advocates in getting new competition into defense procurements?

General SKANTZE. The Air Force formally established its Competition Advocate Program in January 1982. The program was emphasized and expanded as a result of recommendations in the Air Force Management Analysis Group report issued in October 1983. An effective increase in competition requires increased emphasis on programs in the development phase. Competition increased during fiscal year 1985 as a result of this increased emphasis on major production programs and on spares competition and breakout. In terms of number of actions, 82% of 3.4 million procurements were competitive. In terms of dollars, 39.2% of the Air Force procurements were competitive awards. Follow-on contracts to production programs originally competed accounted for another 48%. Only 12.8% of the procurement dollars was awarded through new sole source contracts. The momentum for the Air Force Competition Advocate Program is still growing. The projections in our command competition plans are forecasting even more success in fiscal years 1986 and 1987.

NAVY RESPONSE. Although our reporting system does not capture data regarding new competitors, we can cite specific instances of first time Navy contractors and companies other than the incumbent being competitively awarded previously sole source Navy contracts. Examples include:

During fiscal year 1985, new ship construction or conversion contracts were awarded to five shipyards which had no new Navy construction awards in fiscal year 1984.

Competition for the A-6 attack aircraft replacement wings resulted in an award to a company other than the manufacturer of the A-6 aircraft.

Competition for an improvement to the AN/SLQ-32 electronic countermeasures set was won by a contractor other than the original developer/producer.

The Navy is committed to enhancing procurement opportunities for small and disadvantaged businesses. During fiscal year 1985, the Navy increased contract awards to small businesses by $943 million, a 15 percent improvement over fiscal year 1984. Awards to disadvantaged businesses increased 44 percent over the previous fiscal year.

The Competition Advocate General of the Navy meets regularly with companies seeking advice on ways to obtain Navy business. Competition advocates at each of our major buying commands provide information relative to upcoming competitive opportunities upon request. The Navy is not seeking a specific increase in the number of new firms obtaining Navy business. Our objective is to achieve the benefit competition provides. We increase the opportunities available to obtain Navy business, and marketplace competition will determine which companies are successful in obtaining Navy business.

The Navy is obtaining the "best value" for the taxpayer's dollars as a result of competition. Our experience has shown that competition provides lower costs, better cost control, improved schedules, higher quality, increased contractor responsiveness, and a stronger industrial base. Some examples of savings from competition include:

More than $2.5 billion savings from shipbuilding competition during fiscal year 1983-1985, including $248 million in the SSN-688 class attack submarine program and $840 million in the CG-47 class Aegis cruiser program.

$362 million savings for the A-6 aircraft replacement wings.

For the same item, replenishment spares bought by the Navy Ships Parts Control Center in fiscal year 1985 cost 12 percent less on average than spares bought in fiscal year 1984.

Greater than $520 million cost avoidance during fiscal year 1984-1985 from Project BOSS (Buy Our Spares Smart) initiative. Based on an investment of $101 million, this represents a return of almost 5:1.

The Navy has been at the forefront of the Defense Department efforts to increase procurement competition. In July 1983 the Secretary of the Navy installed a flag officer as the Competition Advocate General—the first such position in the Defense Department—who is supported by a network of over 250 command competition advocates. The emphasis placed on Navy procurement competition by the Secretary of the Navy and the Chief of Naval Operations has created a climate which encourages excellence in procurement and cost-sensitive management of our acquisition programs. The actions of top Navy leadership have brought about the desired results achieved by the Navy acquisition team of program managers, contracting officers, competition advocates, and other acquisition professionals. In fiscal year 1985, 45 percent of contract dollars and almost 70 percent of all contracts actions were awarded competitively. Compared to fiscal year 1984, this performance represents:

A 21 percent improvement in percentage of dollars awarded competitively;

A 39 percent improvement in dollar amount of competitive awards;

A 38 percent improvement in percentage of contract action awarded competitively;

In fiscal year 1985, we awarded $20.2 billion competitively, a $10.8 billion increase over fiscal year 1982. Thus, in fiscal year 1985 industry was able to compete for more than twice the amount of awards available in fiscal year 1982.

COMPETITION VERSUS QUALITY

Senator LEVIN. In Dr. Wade's statement, he notes the need to ensure that the Department builds or maintains high quality into the systems and parts that you purchase. Do you see any diminution in your service's ability to obtain quality products and services while at the same time undertaking an aggressive competitive program?

General **Skantze**. Unequivocably no. The alternate fighter engine (AFE) competition is an excellent example where the Air Force obtained strong competition and significantly improved reliability from both Pratt & Whitney and General Electric.

Navy Response. The Navy has placed a high priority on quality and takes remedial actions as appropriate to hold the line on quality. Problems with quality occurred occasionally before the increased emphasis on competition and occasional problems occur today. However, there is no indication of a direct relationship between quality problems and competition. There has been no increase in the number of Quality Deficiency Reports. First Article Test results have improved at the Aviation Supply Office, which has competed many critical aircraft components that were previously bought sole source. The Navy is currently competing 45 percent of all procurement dollars and seven of every ten procurement actions, and fleet readiness remains high. From evidence discussed in competition literature, there are indications that competition can contribute to quality improvements. Historical competition programs such as the AIM-7F Sparrow missile have employed competition during the acquistion process to specifically improve quality. The AIM-9M Sidewinder missile, competed between Raytheon and Ford Aerospace, has exceeded reliability goals by 100 percent and production verification test requirements by 400 percent. Other Navy programs have been successfully competed without any degradation in quality. These include: the SSN-688 class submarine, the FFG-7 class frigate, the Cruise missile engine and inertial navigation system, and the armoured box launch system.

WORK MEASUREMENT STANDARDS

Senator **Levin**. One of the issues which the Congress has been facing recently is the need to collect information on a contractor's work measurement goals and achievements.

Do you now routinely request this information from contractors?

General **Skantze**. Air Force contractors routinely provide cost, price, and performance data (which includes work measurement data) in support of their contract proposals. During contract performance Air Force representatives have access to contractor management and performance records. However, a system does not exist for collecting, formatting, and summarizing cost, price and performance data. Air Force information systems do track contractual and budgetary actions on a service wide basis. In addition, when cost type contract instruments are used, contractors are required to report cost performance against both budget and schedule.

Senator **Levin**. If this information is made available to you, how is this information used by your service?

General **Skantze**. Proposal, negotiation, and performance data is routinely based on an individual contractor, his subcontractors, and the unique program they are supporting. Evaluation of contractor generated data requires a thorough knowledge of the contractor accounting systems used, the design and manufacturing limitations, and the economic environment in which the prime and the subcontractors are working. Air Force program offices and government contract administration offices work directly with contractor generated records and documents to analyze cost proposals and monitor contractor compliance with contractual commitments.

Senator **Levin**. If this type of information collected from contractors was expanded, how would you take advantage of the additional information?

General **Skantze**. If the Air Force is able to collect all the data required by the fiscal year 1986 Authorization Act, cost and price legislation, we do not know what advantage if any will be gained from that additional information. The resources expended by program office, government contract administration, and contractor organizations which would be required to collect, reformat, and summarize contractor data would reduce the dedication of those resources to the detailed analysis of said data and other procurement responsibilities. As a result, the field resources currently expended negotiating and monitoring contracts would be spent reformatting contractor data. An alternative solution would be to pay all of our contractors to standardize their accounting and work measurement systems.

The Air Force firmly supports and has taken the lead in the use of work measurement standards on government contracts. Currently, over seventy percent of Air Force Major Programs have MIL-STD-1567A, Work Measurement, on contract. Where available, the data generated by contractor work measurement systems has been used in contract negotiations.

Navy Response. The Navy receives standard labor data on a number of programs, primarily missiles and electronics. While we do not routinely request information on a contractor's work measurement goals and achievements, we do request such information when we need this information to negotiate reasonable prices. In other instances, where contractors have some form of this data available, we look at it on a case by case basis. We believe that work measurement standards apply to an ever decreasing percentage of contract cost (labor, for example), and as such, the potential impact is limited. In many instances, decreasing unit costs due to the proper effects of learning are better measurement bases for analysis and negotiation than are standard hours.

Some specific concerns are as follows:

Techniques for developing standards for large-scale production cannot successfully be applied to small scale production runs characterisic of much defense manufacturing.

Work measurement standards cannot successfully be applied to non-production endeavors such as research and development, engineering support and production management.

Many programs have sufficient actual history to propose, evaluate and negotiate reasonable prices on the basis of actuals—requiring these programs to establish work measurement standards would not improve the ability to negotiate lower prices and would not be cost effective to implement.

As the Navy moves more and more to competition, the need for either standard hours or excessive amounts of data with associated preparation costs declines drastically. This information is only useful in a sole source, negotiated environment, and then only in some circumstances.

REVOLVING DOOR

Senator LEVIN. You talked about the importance of a well-trained and motivated procurement workforce. As you know, the debate is continuing in the Congress on an appropriate governmental policy for the "revolving door."

Do you believe that individuals in the DOD acquisition work force should be automatically precluded from going to work with a defense contractor solely because of the position that the individual holds within DOD?

General SKANTZE. No, they should not be precluded from post DOD employment solely because of the position they hold within DOD. What should be firmly prohibited is the DOD employee's use of his/her government position or influence resulting therefrom (i) for personal gain, (ii) to the detriment of the Government, or (iii) in a manner which gives an unfair advantage to a private entity.

Senator LEVIN. What do you believe an appropriate "revolving door" policy for contracting personnel in your service should be?

General SKANTZE. The laws existing prior to Public Law 99-145 prohibit former officers and employees from improper use of their influence or position. Those laws were carefully written to balance the right of the individual to try to make a living against the right of the public to be assured that official relationship will not be improperly exploited. Therefore, the policy existing prior to Public Law 99-145 should apply.

Senator LEVIN. Should this "revolving door" policy be applied only against DOD employees, or should it be applicable government-wide?

General SKANTZE. Government-wide, the majority of the provisions in the existing laws regarding "revolving door" apply to all government personnel. Any new provisions should apply to all employees of the executive, legislative and judicial branches.

NAVY RESPONSE. Navy believes post Government employment opportunities with a defense contractor should not be limited solely by a position held prior to leaving the Department of Defense (DOD). Navy policy requires individuals considering post government employment with a particular defense contractor to disqualify themselves immediately from any involvement in matters associated with that contractor.

Any "revolving door" legislation should be equitably applied government wide to those individuals who have significant influence on the acquisition process in either program development, execution or funds appropriation.

TRANSLATING LEGISLATION INTO IMPLEMENTATION

Senator LEVIN. In your statements, you indicated that the enactment of legislation is only the starting point for the implementation of changes within the procurement system. What would the normal flowchart and timetable be within your service for a legislative requirement to go from enactment in Washington to implementation at one of the buying centers?

General **Skantze**. The normal flowchart and timetable to implement a Department of Defense or Government-wide legislative contracting requirement at Air Force buying activities is as follows:

Flowchart process	Timetable (rough estimates)
1. Receipt of statute by Department of Defense, Defense Acquisition Regulatory [DAR] Council and development of a DAR case.	1–30 Days.
2. Assignment of case by DAR Council to a DAR Council Committee for development of proposed Federal acquisition regulation [FAR] or DOD FAR supplement coverage.	7–14 days.
3. Preparation of report by DAR Council Committee	30–60 days.
4. DAR Council revision/approval of committee report	30–60 days.
5. For Government-wide requirements submission of DAR Council approved coverage to the Civilian Agency Acquisition [CAA] Council for review/approval.	30–60 days.
6. Resolution of any disagreements between DAR and CAA Council	30 days.
7. Publication of proposed rule in the Federal Register as required by Public law 98–577, along with Regulatory Flexibility Act (Public Law 96–354) notice of proposed rulemaking.	Minimum 30 days (waivable when urgent and compelling circumstances make it impracticable to obtain public comment prior to the regulation becoming effective).
8. When the proposed rule requires collection of information from offerors, contractors and members of the public, an Office of Management and Budget control number must be obtained for display on the information collection request in accordance with the Paperwork Reduction Act (Public Law 96–511).	30 days (can overlap step 7 time. This time is, therefore, not included in the cumulative total).
9. Resolution of public comments by DAR and CAA Councils, including referral of comments to committees for preparation of a report to the DAR Council and consideration of the Committee report by the DAR and CAA Councils.	30–60 days.
10. Publication of final rule in the Federal Register	10 days.
11. Publication of rule in loose-leaf version of FAR or DOD FAR supplement by the Government Printing Office and distribution to subscribers.	30–45 days.
12. Receipt by HQ USAF of Government or DOD-wide regulatory coverage and development of USAF implementing regulatory coverage (e.g., delegations of authority and approval levels).	30 days.
13. Receipt of regulatory coverage by Air Force buying offices and development of local procedures, forms, revision of master solicitations, revision of automated systems, and the like, as applicable.	30–60 days (if automated systems changes are required, as much as 9 mo to a year may be required).
14. Distribution of changes and training and indoctrination of buying personnel on the new regulatory requirements.	1–10 days initially, but this is a continuing iterative process based on experience in practice and GAO and Court decisions.
Total	289–499 days.

Navy Response. The Implementation of legislation within the procurement system is divided into three distinct phases. These are (1) the drafting and approval of regulations by the DAR Council; (2) the printing and distribution of the regulations; and (3) the actual implementation in the field including training, development of new or revised local procedures and delegations of authority or approval levels.

The most visible part of this process is the drafting and approval of regulations by the DAR Council. This portion involves a nominal 260 days for a change to the Federal Acquisition Regulation (FAR) and 170 days for a change to the DOD FAR Supplement (DFARS). These are average times which can vary considerably depending on the complexity of the change. These time frames are developed as follows:

	FAR		DFARS	
	Event	Cumulative	Event	Cumulative
Receipt of Statute by DAR Council and development of a DAR Case	10	10	10	10
Assignment to DAR Council Commmittee and receipt of recommended coverage	30	40	30	40
DAR Council review/revision/approval	30	70	30	70
Submission of DAR Council approved coverage to Civilian Agency Acquisition Council (CAAC) and resolution of any disagreements	60	130	0	70
Publication of proposed rule in Federal Register for public comment	70	200	70	140

	FAR		DFARS	
	Event	Cumulative	Event	Cumulative
Analysis of public comments, coordination with CAAC, and approval of final rule...	60	260	30	170

The next phase of the process is the printing of the approved coverage in a Federal Acquisition Circular (FAC) or a Defense Acquisition Circular (DAC) and publication in the Federal Register. While this process can be shortened in an emergency, it cannot be done as a standard practice as distribution to all users of the regulation is only ensured through the standard process. The Navy, for example, requires over 5,000 copies of the changes. The time frames for this phase are as follows:

	Days
Printing of a FAC or DAC	90
Publication of final rule in the Federal Register. (Done in parallel with printing).	10
Distribution to field activities and other subscribers	90

The third phase of the process is the actual implementation by the field. This includes training of personnel in the new regulations, delegations of authority and the development of new or revised local procedures as appropriate. It could include changes to automated systems, revisions to standard solicitation and contract drafting procedures or changes to approval levels or procedures. The time frame for this phase is extremely variable and can run from 30 days to one full year.

From the above, it is readily apparent that implementation of legislation can take from 1 year to over 2 years depending on the complexity of the change and the activities and systems affected.

There is also a fourth phase to this process that results from actual experience with the new regulations and GAO, ASBCA, GSBCA and court decisions. For many changes, this phase extends a number of years in order to fully understand the impact of the change and to amend the regulations to assure proper implementation.

DATA RIGHTS FOR REPROCUREMENT PURPOSES

Senator LEVIN. What steps are you taking at AFLC today to address the issue of obtaining data rights for reprocurement purposes?

General O'LOUGHLIN. We actually have two programs, one to assure that there are no unresolved data rights issues in our present ongoing programs and the other to resolve data rights issues on data delivered over the last twenty-five years.

In conjunction with AFSC, we challenge all data rights limitations before the data is delivered on ongoing programs. We also audit all drawings to assure completeness and accuracy.

In the other program, we actively pursue release of rights limitations on existing data if the data could otherwise be used to compete a spare part. We have a five-step challenge procedure which begins with an informal request/challenge sent to the contractor and ends with a formal challenge issued by a procurement official if earlier steps are not fruitful.

Senator LEVIN. Of the 133 data rights releases obtained by Warner Robins ALC, mentioned in your statement, how many of these releases resulted from some type of formal data rights challenges?

General O'LOUGHLIN. All of the 133 releases resulted from the first step informal request/challenge of the five-step challenge procedure.

Senator LEVIN. Of the 54 instances where Warner Robins had to pay for data rights, what was the range of prices paid for those rights? Were these prices negotiated "up front" during initial contract negotiation or as a contract modification?

General O'LOUGHLIN. Thus far, 14 of the issues have been negotiated at prices ranging from $177.23 to $966,000. The latter is a satellite tracking antenna system consisting of numerous drawings. All of this data was from completed (old) contracts so separate contracts and negotiations were necessary. The remaining 40 issues are still in contract or negotiation process.

Senator LEVIN. What has been the experience in obtaining the release of data rights at other AFLC installations?

General O'LOUGHLIN. The five Air Logistics Centers have experienced relative success with the informal first step procedure. Accurate records of actions taken and successes were not previously kept so we do not have figures that we can quote.

CAUSES FOR PROCUREMENT PROBLEMS IN SPARE PARTS PRICING

Senator LEVIN. In your statement (p 16) you indicate that a number of management policies, procedures and manpower contribute to the difficulties in addressing the causes for procurement problems in spare parts pricing. What are some of those policies and procedures? Have these been addressed legislatively or resolved administratively yet?

General O'LOUGHLIN. In the past, manpower shortages have been a major impediment to our efforts to achieve fair and reasonable spare parts pricing. In fiscal year 1982, for example, AFLC contracting was allocated only 78% of their manpower requirements. The result of manpower shortages of this magnitude is that individual workloads become excessive. Consequently, we concentrated on the higher dollar value contracts: those contracts which individually obligate more than $100,000 each and which, collectively, account for over 90% of our total obligations even though they are less than 15% of our total contract actions. Also, our pricing efforts were directed at obtaining a bottom-line objective on each contract—achieving an overall good deal, but not paying much attention to individual line item distribution of costs, and hence, prices.

However, AFLC no longer faces as severe manpower shortages as past years. In fiscal year 1986, AFLC contracting is manned at 86% of our requirements. Consequently, we now have the manpower to support the various initiatives we started in fiscal year 1983 to improve spare parts pricing. These include: an actual value review of each item, to be sure a good relationship exists with its price tag; a pricing technique (Spares Management Analysis and Review Technique—SMART) we developed to assist the buyer for those negotiated purchases which do not require the contractor to give us certified cost and pricing data; another pricing technique, called PARTS (Price Analysis and Review Technique for Spares), which is applied to those larger purchases with many separate items and ensures each and every line item is value reviewed. The increases in contracting manpower we received in fiscal year 1984 and fiscal year 1985 have enabled us to effectively implement these improved pricing initiatives. Achieving adequate manning will enable us to institutionalize these significant policy changes.

Another major impediment to effective pricing that was faced by AFLC in recent years was funding shortfalls. Underfunding creates a number of pricing related problems. One is that we are unable to buy in large, economical order quantity lots. Thus, we are unable to take advantage of quantity price discounts as well as other cost savings associated with increased contracting efficiency. Funding shortfalls also inhibited our use of multi-year contracting, and the associated pricing benefits of increased competition, reduced start-up costs, improved productivity, and program stability.

As a result of improved funding, we have been able to buy many more of our requirements once a year. We have also expanded our use of multi-year contracts.

In the past, we've bought a lot of items directly from prime manufacturers when they are not the actual producers. The usual result of such arrangements has been higher prices than if we'd bought from the actual producer. This is because the primes normally add their own overhead and profit charges to the producers' costs. When the primes add nothing of value to the items then these added charges are, in effect, unearned profits, and result in higher prices. We had long been aware of this problem, and, in fiscal year 1983, began to "break out" items to the actual manufacturer. Although some contractors were reluctant to identify the actual producers of no value-added items, most contractors were very cooperative. P.L. 98–525 gives us the necessary statutory muscle to obtain this information in those instances where the contractor will not cooperate.

In addition to pricing-related initiatives, we have been able to begin to upgrade our 1960's vintage data management systems. We have beefed-up our up-front acquisition planning and business strategy. We have improved our capability for developing additional sources for competition purposes and for identifying actual manufacturers and buying direct from them. We're also encouraging contractors to get involved in submitting value engineering changes, and we've made the zero overpricing program more responsive to Air Force users of spares. These are examples of the initiatives we've taken to improve the pricing of spare parts.

All the initiatives we've taken to improve the buying of spare parts are resource related. Efficient and effective contracting depends upon the continued availability of adequate resources to carry out the policy and procedural changes we have instituted over the past 2 years.

UNPRICED ACTIONS TO MEET LENGTHENING LEADTIME

Senator **Levin**. In your statement (p 34) you inidicate that: to offset unanticipated lead time increases as well as unanticipated needs, and to avoid supply support gaps downstream . . ., using unpriced actions becomes essential. Is the use of unpriced actions growing within AFLC? Within the Air Force? Is the use of unpriced actions the only reasonable action that AFLC can take to address the growth in administrative lead time?

General **O'Loughlin**. Undefinitized Contractual Actions (UCAs) are an essential tool in reducing the length of the acquisition process in order to meet urgent requirements need dates, to avoid production breaks or to ensure that timely action is taken to avoid government injury. Both the issuance and on-hand balance of UCAs have increased within AFLC. This growth is primarily attributable to a significant increase in Contracting Administative Lead Time (CALT), the time from identification of a requirement in contracting until contract award.

Contracting administrative lead time has increased from an average of 54 days in FY81 to a peak of 133 days in mid FY85. The nature of our business has changed dramatically over the last three years. We have had to implement and institutionalize over 85 regulatory changes and a multitude of acquisition process and systems changes. These changes coupled with a 65 percent increase in obligations since FY81 and extreme caution by government and industry contracting personnel significantly slowed the process.

UCA issuance is not a means of addressing the growth in CALT, rather it is a result of this growth. Requirement identification must now be accomplished much earlier to ensure item availability when needed. Urgent requirements have increased to 27 percent of our workload. The increased time to fill needs has increased the visibility of perturbations in failure or condemnation rates. UCA issuance will remain a necessity to: ensure valid urgent requirements are met, FMS country-directed need dates are met, and to correct safety of flight deficiencies.

AFLC has implemented stringent measures to reduce the effects of increasing CALT. In FY84 we began an aggressive nationwide recruiting program, resulting in the hiring and training of over 300 new contracting personnel. This program has been repeated two more times, bringing a total of 956 trained contracting personnel into the Command. AFLC also instituted a number of changes to buy individual items in larger quantities less frequently; for example, buying an item more than once a year. Additionally, purchase requests are being initiated earlier to allow sufficient time between receipt of requirements in contracting offices and contract award.

Senator **Levin**. What has been the AFLC prior use of unpriced actions? What are the policies and procedures with AFLC to definitize unpriced actions?

General **O'Loughlin**. UCA issuance has averaged approximately one percent of our actions and 26.6 percent of AFLC dollars obligated, over the past five years. Several new management and policy controls have been implemented to ensure a reduction in issuance and in on-hand balances. Approval levels for UCA issuance have been increased. Additionally, the practice of combining routine items or quantities with urgent requirements will no longer be used unless significant savings can be achieved by doing so.

Definitization is the key to controlling UCAs and is being strongly emphasized. Goals for on-hand balances are being established for each ALC. Progress on open actions against milestone dates will be tracked monthly on a contract by contract basis by upper level management. AFLC has also instituted several new management controls and policies on definitization, which include: no order will have greater than a 180 day definitization schedule, no more than 50 percent of the action's "not to exceed" amount may be obligated on an action without Head of Contracting Activity approval and a firm priced proposal must be received prior to issuance unless compelling reasons warrant waiver of this requirement by the ALC Commander.

GENERAL AND ADMINISTRATIVE EXPENSES INCLUDED IN PROFIT CALCULATIONS

Senator **Levin**. During our Acquisition Subcommittee hearings earlier this year, I questioned DOD officials and Defense contractors about the current Department of Defense markup policy. Under your rules, you permit Defense contractors to earn a "profit" based in part on size of the contractor's general and administrative expense. In my judgment, this offers the contractor an incentive to increase costs.

I offered an amendment which has been included in the fiscal year 1986 DOD Conference report (section 903) which asks for a report by the Secretary of Defense on the desirability of continuing the current policy.

Since that time, the Department's DFAIR study has been released. In that study, the DFAIR team noted:

"An argument can be made for excluding G&A from the markup base. If excluded, any incentive provided by the markup policy for contractor to increase G&A costs would be removed."

Could you support a change in DOD policy which excludes G&A from the markup base for your service?

If you agreed with such a change, would such an action require legislation or could it be done administratively?

General Babers. G&A is a normal business expense. Eliminating G&A from the base could result in contractors attempting to negotiate higher profit factors for labor effort, purchased parts, or other areas related to the manufacturing process. Contractors want to maintain a certain overall return on investment/return on assets regardless of the profit factor on individual contracts. Making defense business less attractive could erode the industrial base needed for a competitive defense market.

AGENCY PURCHASING OFFICERS' MORALE

Senator Levin. In a recent interview, one of the OSD acquisition deputies stated that the morale of the acquisition workforce had "sunk so low they don't talk to their relatives about it."

Do you share that view of the morale of the Department's and your service's acquisition workforce?

Don't events such as the Navy Secretary's precipitious action to fire the three officials at the Miramar Naval Air Station contribute to the workforce's fear of either making a mistake or overpaying for some parts?

What actions has your Service taken to enhance the professionalism of the workforce?

General Babers. The morale of DLA buyers has been affected by events over the last several years and some are afraid to sign awards in the face of possible punitive action if they make an incorrect pricing decision.

A number of actions have been taken to enhance the professionalism of the DLA Contracting workforce. (1) A standard program of classroom instruction and on-the-job training has been developed for contracting personnel. All future entry level buyers will complete this standard program. An important aspect of this program is a new course in spare parts small purchase pricing (presently under development). This course will teach buyers how to resolve the type of pricing problems that are unique to small quantity, small dollar purchases. (2) Buyer position descriptions have been revised to remove all semblance of clerical work. Duties such as abstracting offers and document preparation have been transferred to clerks. DLA buyers will function solely as decision makers and problem solvers. (3) Implementation of an internal training program is underway. It has been designed to identify specific knowledge/skills deficiencies of individual buyers. These deficiencies will be corrected through the use of module type training with written examination. (4) A DOD mandatory training shortfall of approximately 4800 course requirements was identified at the end of fiscal year 1984. Over 50% of that shortfall has already been eliminated and we expect to eliminate the balance by the end of fiscal year 1986.

PENALTIES FOR CONTRACTORS

Senator Levin. Included in the FY86 DOD conference bill are a number of significant penalties that will be imposed on defense contractors for submitting false claims, and overcharging for work, for example.

Do you believe these penalties will act as an effective deterrent to fraud for contractors doing business with the Pentagon? Should these penalties be applicable to any contractor doing business with the Federal government, not just DOD?

Are these sanctions enough of a deterrent for DOD contractors?

General Babers. It is too early to make any judgements on the possible success of the new penalties or their possible application Government-wide.

There already is an existing array of criminal, civil, and contractual measures that can be taken to protect the Government's interests and deter fradulents acts by DOD contractors. DLA has taken debarment action, obtained financial recoveries and obtained corrective measures by contractors using these existing remedies.

The efficacy of the new penalties will depend partly on the implementing regulations and the interpretations given to them by the courts. Further, if the penalties are perceived as disproportionate to the alleged offense they may serve as more of a deterrent to participating in DOD procurements than a deterrent to fraud.

Similarly, it is premature to assess the benefits of applying these penalties throughout the Federal Government. As experience is gained from DOD's efforts, there will be opportunities to consider applying these penalties throughout the Federal Government, either by new legislation or possibly by Government-wide regulations.

COMPETITION

Senator **Levin**. One of the goals of the 1984 legislation was to open up the Federal procurement process to new players, particularly small and minority business.

Have you seen an increase in the number of new competitors for many of your service's purchases? Is your service getting a better deal for its dollar because of this new competition?

As part of the 1984 legislation, Congress formally established the Competition Advocate program. How successful are the competiton advocates in getting *new* competition into defense procurements?

General **Babers**. Due to the diverse and dynamic nature of bidder's mailing lists, and the large volume of firms involved in our competition outreach efforts, tracking new bidder participation is not currently accomplished. However, an indicator of additional sources can be noted by changes in the competitive status of items as a result of the availability of technical data. In fiscal year 1985, 2,189 were changed to become suitable for competitive acquisition as a consequence of competition breakout actions

During fiscal year 1985 DLA compiled savings in excess of 167 million dollars as results of spare parts, pricing and competition initiatives. The savings will be reflected on future reductions in the standard unit prices of items required by the Military Services.

The competition advocates are very successful in getting new competition. The DLA competiton dollar rate increased at a steady rate since fiscal year 1983. The overall increase from fiscal year 1983 to fiscal year 1985 was 10.3%. The Agency has surpassed its goal each year. DLA's competitive action rate has increased by 18.5% for the same period.

COMPETITION VERSUS QUALITY

Senator **Levin**. In Dr. Wade's statement, he noted the need to ensure that the Department builds or maintains high quality into the systems and parts that you purchase. Do you see any diminution in your Service's ability to obtain quality products and services while at the same time undertaking an aggressive competitive program?

General **Babers**. Although we have not tracked effects on quality to date, we expect to perform a study to determine the effect of the Competition Advocate program on quality early in fiscal year 1987. The reason for deferring this study until that time is that DLA has recently embarked on an aggressive program to emphasize quality. The agency has, therefore, educated Military customers in the submission of reports on poor quality. Consequently, the volume of such reports and returns are expected to increase dramatically.

WORK MEASUREMENT STANDARDS

Senator **Levin**. One of the issues which the Congress has been facing recently is the need to collect information on a contractor's work measurement goals and achievements.

Do you now routinely request this information from contractors?

If this information is made available to you, how is this information used by your service?

If this type or information collected from contractors were to be expanded, how would you take advantage of the additional information?

General **Babers**. Only when Military Standard (MIL-STD) 1567A, Contractor Work Measurement is included as a provision in the contract.

When MIL-STD-1567A is in the contract, it requires the contractor to have a work measurement system. Likewise, it requires the contractor to use engineered standards instead of historical data for manufacturing planning, proposal preparation, methods improvement, and identifying resource requirements. Expanded information is not required for contractors who meet the criteria for MIL-STD-1567A.

REVOLVING DOOR

Senator Levin. You talked about the importance of a well-trained and motivated procurement workforce. As you know, the debate is continuing in the Congress on an appropriate governmental policy for the "revolving door."

Do you believe that individuals in the DOD acquisition workforce should be automatically precluded from going to work with a defense contractor solely because of the position that that individual holds with in DOD?

What do you believe an appropriate "revolving door" policy for contracting personnel in your service should be?

Should this "revolving door" policy be applied only against DOD employees, or should it be applicable government-wide?

General Babers. We do not feel that the DOD Acquisition workforce should be automatically precluded from going to work for defense contractors. In our experience, positive benefits to the Government have resulted from cross fertilization, particularly when one of our employees joins a small business firm.

If new legislation is enacted, it should address the revolving door problem. Government employees should not represent the Government one day on contract or contract related matters and the Company the next. This prohibition should apply Government wide, regardless of grade or position, and serve as a cooling off period for a least a year with regard to companies the employee has done business with as a Government official.

TRANSLATING LEGISLATION INTO IMPLEMENTATION

Senator Levin. In your statements, you indicated that the enactment of legislation is only the starting point for the implementation of changes within the procurement system. What would the normal flowchart and timetable be within your service for a legislative requirement to go from enactment in Washington to implementation at one of the buying centers?

General Babers. The normal flowchart and timetable to implement a Department of Defense or Government-wide legislative contracting requirement at our buying center is as follows:

Flowchart process	Timetable (rough estimates)
1. Receipt fo statute by Department of Defense, Defense Acquisition Regulatory [DAR] Council and development of a DAR case.	1–30 days.
2. Assignment of case by DAR Council to a DAR Council Committee for development of proposed Federal Acquisition Regulation [FAR] or DOD FAR supplement coverage.	7–14 days.
3. Preparation of report by DAR Council Committee	30–60 days.
4. DAR Council revision/approval of committee report	30–60 days.
5. For Government-wide requirements, submission of DAR Council approved coverage to the Civilian Agency Acquisition [CAA] Council for review/approval.	30–60 days.
6. Resolution of an disagreements between DAR and CAA Council	30 days.
7. Publication of proposed rule in the Federal Register as required by Public law 98–577, along with Regulatory Flexibility Act (Public Law 96–354) notice of proposed rulemaking.	Minimum 30 days (waivable when urgent and compelling circumstances make it impracticable to obtain public comment prior to the regulation becoming effective).
8. When the proposed rule requires collection of information from offerors, contractors and members of the public, an Office of Management and Budget control number must be obtained for display on the information collection request in accordance with the Paperwork Reduction Act (Public law 96–511).	30 days (can overlap step 7 time. This time is, therefore, not included in the cumulative total).
9. Resolution of public comments by DAR and CAA Councils, including referral of comments to committees for preparation of a report to the DAR Council and consideration of the Committee report by the DAR and CAA Councils.	30–60 days.
10. Publication of final rule in the Federal Register	10 days.
11. Publication of rule in loose-leaf version of FAR or DOD FAR Supplement by the Government Printing Office and distribution to subscribers.	30–45 days.
12. Receipt by DLA Headquarters of Government or DOD-wide regulatory coverage and development of DLA Headquarters implementing regulatory coverage (e.g., delegations of authority and approval levels).	30 days.

Flowchart process	Timetable (rough estimates)
13. Receipt of regulatory coverage by DLA buying offices and development of local procedures, forms, revision of master solicitations, revision of automated systems, and the like, as applicable.	30–60 days (if automated systems changes are required, as much as 9 months to a year may be required).
14. Distribution of changes and training and indoctrination of buying personnel on the new regulatory requirements.	1–10 days initially, but this is a continuing iterative process based on experience in practice and GAO and Court decisions.
Total	289–499 days (add a minimum of an additional 210 days for some automated system changes to be made).

COMPETITION HIT LISTS

Senator Levin. General Babers, would you explain your program of "competition hit lists"? How does an item get on the list, and what action does DLA take when items are on the list?

General Babers. Competition Hit Lists are compiled by the various commodities (Hardware Center and DPSC) on items which lack competition, are high demand, and are relatively high cost.

An item is selected for the list due to its sole source nature considering the demand and dollar amount of the item. Items with the largest potential for payoff are coordinated between contracting, supply and technical offices for suitability. Once the item meets the criteria, it is added to the list and remains until competition is obtained or for a given time usually 9 months to 1 year.

DLA distributes the hit lists wherever and whenever feasible. They most notably are given to new contractors at trade fairs and conferences to show the items for which we most need competition.

Continual efforts are made to obtain technical data for the listed items or otherwise improve competition. The lists are also used to entice contractors to "bail" an item or buy the item for reverse engineering purpose.

The lists are also used in the (Defense Contract Administration Services Region (DCASR) network to help potential suppliers identify parts that they can possibly make. Likewise we exchange hit lists among our Supply Centers and distribute them to the Services.

DLA INTRINSIC VALUE ANALYSIS

Senator Levin. As part of your competition advocate program you undertake what you call "intrinsic value analysis." What information do you obtain as a result of this analysis? How broad-based is the screening you do for this intrinsic value analysis"?

General Babers. Our intrinsic value analysis is an engineering estimate of material and direct labor costs for producing specific quantities of the item under review. To this is added a figure to cover overhead cost and profit which is based upon the latest pricing information. The intrinsic value plus the overhead/profit figure, represent a Government estimate of what the item should cost at selected quantities of production. Besides the "should cost" value, our investigations often yield additional information such as potential sources or over-specified design which we pursue for cost savings.

The items referred for intrinsic value analysis are received primarily from two sources: (1) from contracting officers seeking technical assistance in the negotiation of a contract for a sole source item and (2) from price challenges requiring technical review.

The intrinsic value/"should cost" effort, which we have coined "Price Busters" is in its early implementation stage in DLA. We have completed a pilot test at Defense General Supply Center (DGSC) and have recently exported the function to our other Hardware Centers.

For the past 10 months at DGSC, the "Price Busters" group worked on 952 National Stock Numbers (NSNs) from 58 different supply classes. Their reported savings for that period were over $600,000.

QUESTIONS SUBMITTED BY SENATOR JEFF BINGAMAN

MANAGEMENT OF TECHNICAL DATA AND COMPUTER CAPABILITY

Senator BINGAMAN. General Skantze, there are several additional aspects to the problem of technical data. As you know, obtaining the data itself, or at least removing the restrictive legends on that data, is only the first critical step in this important area. Beyond availability, I have focused some attention on the problems of the Department's ability to manage that data and to keep it current. This includes such mundane, but essential requirements as storage, retrieval and tracking.

Do you share my view that the management of the technical data, including indexing, storage and retrieval is as important to the Department as the ability to obtain that data in the first place?

What actions are you taking to better manage the technical data that you now have and that will be obtained in the future?

General SKANTZE. Yes. The Air Force shares your view that the management of the technical data (engineering data) must address all aspects of the technical data program. This would include not only the Department's ability to obtain the data, the rights to the data, and removal of restrictive markings, but also, the storage, retrieval, and tracking of the data. These are all essential requirements, equal in status with the acquisition of data. The marriage of astute data acquisition with efficient management of that data produces cost-effective operation and support of our defense material.

One of Secretary of Defense Weinberger's Directed Spare Parts Initiatives is to automate Department of Defense engineering data repositories. The Air Force response is the Engineering Data Computer Assisted Retrieval System (EDCARS) in conjunction with the Army's Digital Storage and Retrieval Engineering Data System (DSREDS). These are totally new, state-of-the-art systems for storing, retrieving, and transmitting digitized engineering data. This system will revolutionize the techniques and methods of handling and processing engineering data, and greatly enhance the Air Force capability to manage engineering data effectively. The benefits to be realized include:

a. Better tracking of engineering data—no more lost technical data (a closed system—data remains in file)
b. Easier to update the data files with new data or revisions
c. Archival file held off line
d. Less storage space
e. Faster retrieval and distribution
f. Local and remote capability
g. Simple to maintain "backup" file
h. Enhanced competitive procurement of spare parts
i. Greater system flexibility to incorporate future system enhancements
j. Integrated system capability.

EDCARS will give the Air Force the cost-effective, high-technology system it needs for the handling and managing of its engineering data program. In addition, EDCARS will provide an accurate, up-to-date base to make the procurement process more competitive.

MANAGEMENT OF TECHNICAL DATA AND COMPUTER CAPABILITY

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Do you share my view that the management of the technical data, including indexing, storage and retrieval is as important to the Department as the ability to obtain that data in the first place?

What actions are you taking to better manage the technical data that you now have and that will be obtained in the future?

General BABERS. We do, indeed, share your view that the management of the technical data, including indexing, storage, and retrieval is as important to the Department as the ability to obtain that data in the first place.

In that regard, we have taken several initiatives in DLA which we expect to have significant impact on the effectiveness and efficiency with which we manage technical data.

The first of these actions was to contract for automated storage, retrieval, and reproduction equipment for the technical data repositories in each of our hardware—oriented Defense Supply Centers. Installation of this equipment began in November 1985 at the Defense Electronics Supply Center and is scheduled to conclude with the Defense Industrial Supply Center in July 1986. This equipment will virtually eliminate the manual filing, manual retrieval, and manual reproduction functions and reduce the administrative lead time for procurement significantly. Provisions have been made to accommodate and adapt to digital technology when equipment for this purpose becomes available off-the-shelf.

The second action was the formation of an Ad Hoc Committee for the Improvement of Technical Data Management. This committee, whose report has now been submitted and approved, did not focus its attention on studying or redefining the problems, but on solving them. Several of their recommendations are being implemented such as increased staffing, improved grade structure providing a career ladder in technical data, and improved communications within the Technical Data community. The Ad Hoc Committee has been dissolved, but the implementation continues.

The third action in which DLA is currently involved is a complete and comprehensive automted index of technical data in the DOD. Now known by the acronym MEDALS for Military Engineering Data Assets Locator System, this project has been assigned to the Defense Logistics Services Center and is expected to be operational during Fiscal Year 1989. When operational, MEDALS will enable any bona fide user of technical data to quickly identify the location of that data and thereby avoid multiple, fruitless requests.

We are continuing to explore other avenues which offer promise of improvement in our management of technical data both interval to DLA and in concert with the uniformed services and will exploit to the limit those opportunities which are uncovered.

Navy Response. Management of technical data (including indexing, storage and retrieval) is as important as the ability to obtain that data.

Technical data is used in hardware acquisition, maintenance and repair as well as facilities management, spare parts acquisition and training. Present indexing, storage and retrieval is largely performed manually, using hard copy and microfilm. These manual methods provide no capability to interface with new DOD and industry efforts in computer aided design, engineering, manufacturing and logistics; preclude timely access to required data; are susceptible to technical errors; and offer little or no capacity to respond to increasingly complex logistics support requirements.

The Navy has established a project office to coordinate the automation of technical data consistent with other Service/Agency efforts in this area. Their objective is presently being pursued via the following two projects:

EDMICS (Engineering Data Management Information Control System)—A project expected to automate eight engineering drawing repositories and a number of drawing libraries supporting spares acquisition and maintenance. Resultant hardware and software systems will be compatible with other Service/Agency efforts through the use of DOD standards for exchanging technical information in digital form.

NPODS (Navy Print on Demand System)—A project expected to automate high demand DOD military specifications and standards currently warehoused at the single DOD stock point, the Navy Publications and Forms Center, Philadelphia. Such documents are required by DOD and industry organizations supporting acquisition of DOD weapons systems.

Documents can be produced on demand from the on-line data base rather than the warehousing of large publication inventories. Technical data packages needed to support competitive reprocurement of spare and repair parts can be produced in a more timely manner. Out of stock conditions and misfiling of documents virtually can be eliminated. The electronic documents can be indexed according to subject matter or authoring activity, thus supporting on-line access via video display terminals. Revisions to engineering drawings and technical manuals can be transmitted electronically directly to the requesting activity, thus bypassing conventional mail delivery. In short, we anticipate a substantial reduction in job performance time and errors as well as shore based training time.

The immediate availability of accurate data, the increased automation of documents needed for effective logistics support, the substantial reduction in manual functions, and the timely distribution of technical information should make a major contribution to increased productivity.

QUESTIONS SUBMITTED BY SENATOR ALAN DIXON

PREQUALIFICATION OF BIDDERS

Senator DIXON. As part of the legislative package last year, we identified some key barriers to greater participation in the Federal procurement process, including prequalification requirements. We even titled the section on prequalification "encouragement of new competitors." These requirements ranged from the need to be on a pre-approved source list to possessing certain minimum qualifications before being allowed to even receive a solicitation.

I believe that the framework for reducing the use of prequalification requirements established in the bill was correct and manageable. In fact, the regulations are out on the creation and use of new prequalification requirements, and, they appear to track pretty well with what Congress intended. Of course, the proof will be in the implementation.

One area where there is still a problem, however, is addressing the use of existing prequalification requirements. In fact, the 1984 statute explicitly stated that the new prequalification provisions would not apply to these standards which were established by law or regulation before the effective date of the Defense Procurement Reform Act of 1984, i.e. October 19, 1985.

What actions are you taking to reduce the use of prequalification requirements which were in existence on the effective date of the Defense Procurement Reform Act?

General SKANTZE. The Air Force eliminated the use of those prequalification requirements which were in existence on the effective date of the Defense Procurement Reform Act of 1984. Prequalification requirements used by the Air Force procuring activities were cited in the Defense Standardization Manual DOD 4120.3-M. The Air Force supported the Office of the Secretary of Defense in changing the manual to delete the old prequalification requirements and insert the new requirements mandated by the Defense Procurement Reform Act. The new requirements were mandatory for use by all Air Force procuring activities, when Change 4 to DOD 4120.3-M was issued in August 1985.

RELATIONSHIPS BETWEEN THE SERVICES AND SBA BREAKOUT PCR

Senator DIXON. I was interested to hear many of the comments made about the potential for duplication between the role of the Small Business Administrations' breakout PCR (procurement center representative) program and the programs of your individual services.

I was very active in the development of these provisions. It was my understanding, and I believe our intent, that SBA is to be a resource for, not in competition with, the services by identifying items that are potentially capable of being "broken out", and/or identifying firms that are capable of meeting the agency's needs for a particular product or service.

Why do you believe that SBA is a competitor to the Service in its efforts?

General SKANTZE. The SBA is not a competitor per se to the Air Force in its efforts. However, the requirement in Public Law 98-577 to establish breakout procurement center representatives duplicates the functions of Air Force Logistics Command competition advocates.

Senator DIXON. What would you like to see the relationship be between SBA and your Service's breakout and competition advocate functions?

General SKANTZE. The relationship should be complementary. Air Force breakout efforts are concentrated on competition in general. The SBA's resources can be focused more narrowly on individual acquisitions and qualification assistance for small businesses. The SBA's specialized expertise on problems confronting small businesses can contribute another dimension and ensure that small business interests are fully recognized in our breakout deliberations.

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What actions are you taking to reduce the use of prequalification requirements which were in existence on the effective date of the Defense Procurement Reform Act?

General BABERS. The Defense Logistics Agency (DLA) does not have direct authority to place qualification requirements in military specifications. This authority rests with the Military Services Preparing Activities. However, in its role as a Departmental Standardization Office, DLA cooperates with the Defense Materiel Specifications and Standards Office (DMSSO) in enforcing the qualification requirement in the Defense Standardization Manual (DSM) DoD 4102.3-M. This manual requires that every Qualified Products List (QPL) have two or more sources for each product listed. For the past two years (1984 and 1985), DMSSO has requested each Military Department to report QPLs having only single sources listed and to provide complete justification for the retention of a qualification requirement in the military specification for the items.

In the Defense Logistics Agency, the Defense Electronics Supply Center (DESC), as Agent for the Military Services Specification Preparing Activities, has been instrumental in removing the qualification requirement from one general specification and from 13 detail specifications during FY 85. Also, during FY 85, DESC, as Agent for the Military Services Specification Preparing Activities, took action to cancel 74 detail military specifications and 11 sheet form military standards because of a lack of qualified products.

Further, the DSM requires a preparing activity to justify qualification requirements in new specifications and obtain approval from DMSSO before publishing the specification. The policies that govern the establishment of qualification requirements follow for convenient reference:

"Qualification shall be justified in writing when one or more of the following criteria apply and when all conditions in other subsections are met (see 4-200):

a. The time required to conduct one or more of the examinations and tests to determine compliance with all the technical requirements of the specification will exceed 30 days (720 hours).

b. Quality conformance inspection would require special equipment not commonly available.

c. It covers life survival or emergency life-saving equipment. (See FAR 9.304b)

d. The application is critical; failure of the part or equipment would jeopardize successful completion of the mission or pose a significant risk to life or property.

In addition, prior to inclusion of qualification in a specification, the Preparing Activity shall determine that:

a. There is no other practicable way of obtaining conclusive evidence of the availability of products meeting the requirements of the specification in a reasonable time, prior to and independent of acquisition. The requirement for qualification of products shall not be incorporated into a military specification when an impartial industry product certification program exists whose results would provide adequate information.

b. Two or more actual manufacturers are available and willing to submit their products for qualification.

c. Test facilities and resources (normally to be furnished by the product manufacturers) are available to establish and maintain the QPL adequately and without delay.

d. The estimated cost of testing and evaluation has been developed.

When qualification is determined to be required, it shall be included as a specification requirement at the time of initial document promulgation. Specifications shall not be normally revised for the express purpose of including a qualification requirement. In rare instances where it is deemed appropriate to include such requirement in an existing specification, additional justification shall be submitted for approval."

NAVY RESPONSE. Navy activities have completed a review of all prequalification requirements which were in existence prior to effective date of the Defense Procurement Reform Act of 1984, October 19, 1985. We have justified prequalification requirements for those items where needed because of safety, operational testing requirements, or special test equipment application. Where there was only one manufacturer listed, strong technical justification for continuation was required along with action seeking additional competitive sources. Guidelines implementing the Defense Procurement Reform Act of 1984 and improved provisions for control of prequalification requirements are contained in Change 4 to the Defense Standardization Manual 4120.3M dated September 11, 1985.

RELATIONSHIPS BETWEEN THE SERVICES AND SBA BREAKOUT PCR

Senator DIXON. I was interested to hear many of the comments made about the potential for duplication between the role of the Small Business Administration breakout PCR (procurement center representative) program and the programs of your individual services.

I was very active in the development of these provisions. It was my understanding, and I believe our intent, that SBA is to be a resource for, not in competition with, the Services by identifying items that are potentially capable of being "broken out", and/or identifying firms that are capable of meeting the Agency's need for a particular product or service.

Why do you believe that SBA is a competitor to the service in its efforts? What would you like to see the relationship be between SBA and your service's breakout and competition advocate?

General BABERS. There is a responsibility for duplication of effort with SBA because our Competition Advocate, contracting and technical personnel are tasked with identifying items capable of being broken out and with identifying additional potential suppliers. This breakout effort is generally prioritized by potential savings from competition.

Within our Agency, we already have an agreement to avoid duplication of effort. SBA will not "work an item we are already in the process of attempting to break out. We will periodically supply the SBA Breakout Procurement Center representative with a list of items we have worked or are in the process of working. As the SBA program matures, we anticipate that additional local agreements will be common to eliminate duplication of effort between the two Agencies.

NAVY RESPONSE. One Breakout Procurement Center Representative (BPCR) and at least two technical advisors are targeted for placement at eight separate Navy procurement centers. We have little experience in this area upon which to assess the impact of these Small Business Administration assignments. We can make a case that the duties of the BPCRs and their technical advisors will be duplicative of the activities' competition advocates and breakout personnel. Notwithstanding this potential for becoming duplicative of Navy initiatives and contributing to procurement administrative lead time, the program may also offer an opportunity to supplement limited Navy resources with those of SBA. The impact of the program cannot be ascertained until it is fully implemented. We will continue to oversee this program and will provide a follow-up response.

QUESTIONS SUBMITTED BY SENATOR JOHN GLENN

LEGISLATIVE IMPROVEMENTS TO PROCUREMENT

Senator GLENN. I think it is generally agreed that the 1984 procurement legislation was the most substantive change to procurement law since the Armed Services Procurement Act of 1947. In addition to your statements on modifications, I would be interested if you could tell us what part of the 1984 legislation has improved the DOD acquisition process the most, and why?

General SKANTZE. It is too soon to tell what the total impact of last year's procurement reform legislation will be. As a result of the legislation, additional procurement manpower was authorized in all of our organizations with the preponderance going to Air Force Logistics and Air Force Systems Commands. However, the legislative changes were so major it created training problems, not only for the new personnel, but also for our professional work force. Lead time to contract award and consequently deliveries has extended significantly. However, we are still in a learning process and anticipate the lead time being reduced to close to previous levels as experience in the system is gained. Only time will tell what portions of the 1984 legislation improved the DOD acquisition process the most.

NAVY RESPONSE. The Navy supported the Competition of Contracting Act of 1984. The provision requiring justifications and approvals for other than full and open competition procurements have enhanced the effectiveness of our competition advocates. Our commanders and commanding officers are fully aware of their responsibilities for sound business practices, including providing support of the competition advocates.

The Act sent an important message to the acquisition community. Our preferred business practice is competition for the benefits of lower prices, higher quality, and a stronger industrial base.

FLEXIBILITY OF PROGRAM MANAGERS

Senator **GLENN**. There has been concern expressed by many that acquisition reforms may have curbed the flexibility and authority of program managers. In testimony before this subcommittee last week, Dr. Wade stated that our flexibility to take advantage of research and technology may be inhibited by statutory reform. Do you believe that the 1984 legislation has reduced the effectiveness of program managers?

General **SKANTZE**. The 1984 acquisition management reforms have added a significant amount of work for both program managers and procurement personnel. This additional burden has been compounded by the decline in the relative attractiveness of Civil Service pay and benefits and the constant adverse publicity. As a result, we are having problems hiring qualified people particularly in the high cost areas where we try to compete for people. These additional burdens all contribute to further delays in the acquisition process and are perceived by our program managers as impediments to the execution of their responsibilities. These actions also result in a dilution of their authority and subsequent reduction in their flexibility to manage an already complex and time consuming process.

MANAGEMENT OF R&D PROGRAMS

Senator **GLENN**. Many of these same concerns have been expressed about our ability to effectively manage R&D programs. My major concern is the potential impact on several critical R&D programs just getting started, such as SDI, Small ICBM, ATB, and V-22.

General **SKANTZE**. These new programs are some of our first major acquisitions to experience the full impact of the 1984 legislation while they are still in the early development stages. Although we have started these program with a heavy emphasis on competition, we still are experiencing additional delays of up to six months as a result of the legislation. We do expect, however, that these delays are unique to our current situation with implementing the new legislation and believe that these problems will not occur when follow-on programs or other new starts are initiated in subsequent years providing no major changes occur in the law in the near future. Multiple changes to the legislation will only exacerbate the already turbulent situation that now exists. We need the time to evaluate and fully institutionalize the 1984 legislation before we impose more contraints on these and future programs. Once our procurement force is trained and fully qualified regarding the particulars of the law, we can expect minimal problems with implementation.

NAVY RESPONSE. The legislation enacted in 1984 has only been recently implemented. While there is an intuitive feeling that this legislation has reduced the authority and effectiveness of our program managers, we need more time before we can fully evaluate the impact. We will continue to oversee these areas, and will provide a follow-up response.

TECHNICAL DATA

Senator **GLENN**. During the hearing with Dr. Wade, I mentioned that I continue to be concerned about going too far in the area of technical data. The contention of many in industry is that the proposed implementing regulations do not reasonably balance the interests of the government and industry; that they favor government. I am also concerned about the disincentives to industry to conduct private research and development which is absolutely vital to our defense technical base. I would appreciate your views on this matter.

General **SKANTZE**. The proposed implementing regulation that was published in the 10 September 1985 issue of the FEDERAL REGISTER for public comment reflects a rewrite of the Department of Defense Federal Acquisition Regulation Supplement (DFARS) to comply with Public Law 98-525, the Defense Procurement Reform Act, and Public Law 98-577, the Small Business and Federal Procurement Competition Enhancement Act. The proposed regulation seeks to redress an imbalance that in the past has permitted contractors to retain sole-source rights in data into perpetuity without regard to the government needs for competitive reprocurement of spare parts. In some cases, this led to excessive pricing of spare parts as a result of DOD's inability to competitively acquire defense requirements in the open market.

We are aware through discussions and correspondence with industry groups and comments made at the October 1, 1985 public meeting on the proposed regulation that some contractors perceive that the proposed regulation goes too far while others feel the regulation is right on target or perhaps even falls a little short. DOD's objective is to obtain data with unlimited rights where appropriate and to obtain rights in proprietary data where it makes good business sense to do so through such vehicles as licensing, options to purchase and negotiating a time limitation on proprietary rights in technical data.

The public comment period expires January 9, 1986. At that time, DOD will evaluate all public comments and if appropriate modify the proposed regulation to assure an equitable balancing of public and private interests in data pertaining to weapons used for the common defense of our nation.

Navy Response. Regarding a balance of Government and contractor interests, contractors can provide data with limited rights only if the items, components, or processes to which the data pertain were developed at private expense. This requirement has been interpreted to refer to complete development. Under DOD funded development contracts, contractors can, and do, limit the Government's data rights with respect to particular components that were developed exclusively at private expense. The Navy is prepared to pay a fair and reasonable price to acquire rights to permit future competition when it makes sense to do so.

QUALITY IN THE ACQUISITION PROCESS

Senator Glenn. In Dr. Wade's testimony, he stated that competition is "too frequently based on price," and an "award to the low bidder" mentality. He indicated that DOD plans to move away from defining equipment requirements in terms of minimally acceptable terms to the system whereby the best quality equipment at an acceptable price is the recognized objective. I strongly support this objective, but was surprised that this quality issue was not addressed in any depth in any of the statements. I would appreciate your comments on cost versus quality as it relates to the current procurement regulations.

General Skantze. The primary objective of Air Force contracting is to obtain quality goods and services at the lowest reasonable price. The equipment acquired must meet the requirements for which its was intended. It should work but at the same time not require restrictive and unnecessary specifications. The Air Force ensures quality through preaward surveys of contractors' facilities, technical evaluation of the contractors' proposals and quality assurance reviews. Contracts are awarded to the low bidder only if the offeror is technically capable and judged able to produce the required quantities and rates.

Navy Response. The Navy policy is to obtain the maximum benefit from compensation by seeking the "best value" for the taxpayer's dollar. We consider this "best value" to be a combination of competitive price plus demonstrated performance in terms of quality, schedule, technology, or other relevant criteria. In determining our competitive awards, our procurement professionals are guided by not only this Navy policy on best value, but also the Federal Acquisition Regulation, which states in part: "While the lowest price or lowest total cost to the government is properly the deciding factor in many source selections . . . . the government may select the source whose proposal offers the greatest value to the government in terms of performance and other factors." The Navy does not and will not award competitive contracts for products or services without obtaining the requisite levels of quality and reliability, regardless of the prices offered.

The Navy has placed a high priority on quality and takes remedial action as appropriate to hold the line on quality. Problems with quality occurred occasionally before the increased emphasis on competition and occasional problems occur today. However, there is no indication of a direct relationship between quality problems and competition. There has been no increase in the number of Quality Deficiency Reports. First Article Test results have improved at the Aviation Supply Office, which has competed many critical aircraft components that were previously bought sole source. The Navy is currently competing 45 percent of all procurement dollars and seven of every ten procurement actions, and fleet readiness remains high. From evidence discussed in competition literature, there are indications that competition can contribute to quality improvements. Historical competitive programs, such as the AIM-7A Sparrow missile have employed competition during the acquisition process to specifically improve quality. The AIM-9M Sidewinder missile, completed between Raytheon and Ford Aerospace, has exceeded reliability goals by 100 percent and production verification test requirements by 400 percent. Other Navy programs have been successfully competed without any degradation in quality. These include: the SSN-688 class submarine, the FFG-7 class frigate, the Cruise missile engine and inertial navigation system, and the armoured box launcher system. Instead, competition improved quality.

DUAL SOURCING

Senator GLENN. In General Skantze's prepared statement, he indicated that dual sourcing is an excellent technique for reducing program risk and production costs in selected situations, but it is not the panacea that current legislative proposals would lead one to believe. I also read yesterday where the Navy had issued an order directing that all new weapons systems will have two sources. There seems to be a lack of agreement here. I would appreciate your comments on the value of dual sourcing, both the leader-leader approach and the leader-follower approach.

General SKANTZE. As you noted, Secretary Lehman has issued an instruction that emphasizes maximizing the use of multiple sources both before and during full-scale development. And, as stated in my remarks, we also consider multiple sourcing an excellent acquisition strategy in most cases. Like the Navy, we almost always use multiple sources up to Full Scale Engineering Development (FSED), and if funding is available, frequently through FSED as well. Unlike development, however, production multiple sourcing is frequently a more difficult decision, since it is often limited by technical difficulties, quantities and funding.

The leader-leader approach allows us to carry at least two contractors through FSED and initial production, usually with a teaming arrangement. This assures two equally experienced contractors are competing on large dollar production contracts. We have used a variation of this approach on the Combined Effects Munitions Program.

In the case of the leader-follower approach, we require the original development contractor to work with, and help develop, a second production source. This may save funding two contractors during development and initial production, but there may be risks associated with qualifying another source. If the design is not stable, or the drawings not complete, or manufacturing processes not fully disclosed, the "follower" may require some time before being able to compete on an equal basis with the development contractor. This technique is being used on the IR Maverick and AMRAAM programs.

Having stated that, I still believe there are some situations where multiple sourcing should not be used. Obviously on systems with large start up costs and short production runs it will not be cost effective to establish second sources. The current law recognizes that fact. The C-17 and J-STARS programs are recent examples of major systems we believe are not cost effective to dual source.

There may be other reasons as well. Funding constraints sometime make it impossible to carry multiple sources through FSED and initial production. Special classified programs may be difficult to compete if we are trying to limit the proliferation of information. In short, we have to look at each program on a case-by-case basis.

NAVY RESPONSE. The current Navy policy is to compete all new programs and to carry competition forward through the development and production phases, as long as competition makes good business sense. The recent Navy instruction requires each new project/program to begin with a minimum of two contractors/contractor teams performing concurrent but separate development up to full-scale development at which time it will be narrowed to two contractors developing a system to one design. Eventually the two contractors will compete against each other for the major portion of annual production. The instruction provides for exceptions to this policy where the system under development will not be procured in sufficient quantities to warrant dual sources in production.

The development of two or more sources during full-scale development, leader-leader approach, offers the benefit of earlier introduction of production competition into a program, thereby permitting the government to realize maximum savings. The leader-follower approach requires the transfer of technology from one source to another. This approach delays the introduction of production competition into new programs, but is one of the useful techniques for introducing competition into existing production programs.

LEGISLATIVE IMPROVEMENTS TO PROCUREMENT

Senator GLENN. I think it is generally agreed that the 1984 procurement legislation was the most substantive change to procurement law since the Armed Services Procurement Act of 1947. In addition to your statements on modifications, I would be interested if you could tell us what part of the 1984 legislation has improved the DoD acquisition process the most, and why?

General **Babers**. Those parts of the Competition in Contracting Act of 1984 which amended the Armed Services Procurement Act of 1947 to place emphasis in the procurement process on competition, rather than the method of acquisition, have, in general, improved the DLA acquisition process the most. Those amendments have allowed us to concentrate on the more substantive issues of an acquisition, rather than expending time and effort justifying the use of the negotiation method of acquisition.

FLEXIBILITY OF PROGRAM MANAGERS

Senator **Glenn**. There has been concern expressed by many that acquisition reforms may have curbed the flexibility and authority of program managers. In testimony before this subcommittee last week, Dr. Wade stated that our flexibility to take advantage of research and technology may be inhibited by statutory reform. Do you believe that the 1984 legislation has reduced the effectiveness of program managers?

General **Babers**. The Defense Logistics Agency does not employ the title "program manager" in the sense used here. However, we will address the question relative to the "contracting officer's" effectiveness.

Certainly not all of the 1984 procurement reform legislation has reduced the effectiveness of the contracting officer. Some of it has allowed for improving that effectiveness. For example, the provisions of the Department of Defense Authorization Act of 1985 on validation of proprietary data restrictions have given the contracting officer legislative authority to challenge asserted contractor restrictions on rights in technical data.

However, other 1984 procurement legislative reforms have not only reduced, but have eliminated the contracting officer's past authority. The single most significant of these, in our view, is the provision in the Small Business and Federal Procurement Competition Enhancement Act of 1984 which eliminated the contracting officer's historical authority to make the final decision as to the responsibility of a small business firm for small purchases. Under the 1984 law, this decision now rests with the Small Business Administration when we determine a small business offeror on a small purchase to be nonresponsible. As I stated in my testimony, this provision of law diffuses responsibility in assuring that contracts are awarded only to responsible offerors. While the contracting officer is charged with obtaining quality supplies timely, the contracting officer cannot assure that result himself/herself.

MANAGEMENT OF R&D PROGRAMS

Senator **Glenn**. Many of these same concerns have been expressed about our ability to effectively manage R&D programs? My major concern is the potential impact on several critical R&D programs just getting started, such as SDI, Small ICBM, ATB, and V-22.

General **Babers**. The Defense Logistics Agency does not manage R&D programs. Therefore, we do not believe it is appropriate for us to respond to this question.

TECHNICAL DATA

Senator **Glenn**. During the hearing with Dr. Wade, I mentioned that I continue to be concerned about going too far in the area of technical data. The contention of many in industry is that the proposed implementing regulations do not reasonably balance the interests of the government and industry; that they favor government. I am also concerned about the disincentives to industry to conduct private research and development which is absolutely vital to our defense technical base. I would appreciate your views on this matter.

General **Babers**. It would be very advantageous to the Department of Defense if legislative provisions were made for a specific period of time, e.g., seven years from date of any contract, during which the Government would recognize, honor, and protect the valid claim of that contractor that only limited rights in data were transferred to the Government. During that time interval the Government would agree not to disclose the data in question outside the Government for any purpose except in time of war or grave national emergency and only then if that contractor could not deliver sufficient quantities and quality demanded by the response to the war or national emergency. Further, the Government would agree that during the specified time period, it would make no attempt to subvert the contractor's data by any means, e.g., reverse engineering unless the item(s) made using the data in question was subject to a price increase greater than the rate of inflation plus two (2) percent per year. After the specified time has elapsed, the Government must have full and complete rights to the data including the right to release it to any party, domestic or foreign, where the release serves the best interests of the Government.

Data currently in the possession of the Government or coming into the possession of the Government prior to the effective date of the above or in any way not subject to the above, should be deemed free of any restrictions, i.e., the Government has unlimited rights, beginning on the tenth anniversary of its delivery to the Government.

Such a situation affords the contractor greater protection than be now enjoys for seven years or the specific interval selected by Congress, as long as he did not take unreasonable advantage of his situation. Beyond that time, the Government can reduce costs, expand the production base and enjoy the benefits of competition by the use of Unlimited Rights to the data.

In today's rapidly unfolding scientific and technical environment, exclusive use of an idea, part, or process is unlikely to remain the province of any one person, company, corporation, or other entity indefinitely. This proposal offers a fair compromise between the rights of an individual (or other entity) and the needs of the people as a whole represented by the Government.

QUALITY IN THE ACQUISITION PROCESS

Senator GLENN. In Dr. Wade's testimony, he stated that competition is "too frequently based on price," and an "award to the low bidder" mentality. He indicated the DOD plans to move away from defining equipment requirements in terms of minimally acceptable terms to the system whereby the best quality equipment at an acceptable price is the recognized objective. I strongly support this objective, but was surprised that this quality was not addressed in any depth in any of the statements. I would appreciate your comment on cost versus quality as it related to the current procurement regulations.

General BABERS. Current procurement regulations require a contract to be awarded to the low bidder that is both responsive and responsible. By definition, a responsible offeror is one which demonstrates the capability to produce an item to all of the technical requirements and specifications identified in the contract. To further assist the contracting officer in determining that an offeror is responsible and, therefore, that we can expect to get the desired quality, we have developed an automated Quality Evaluation Program (QEP). The QEP is a real time direct access system which is scheduled for implementation at the Defense Supply Center in late 1986. This system will automate the collection of contractor and item histories such as preaward surveys, postaward conferences, waivers, deviations and customer complaints. The system will be readily accessible and will provide quality intelligence to buyers and contracting officers for use in the preaward contracting process so as to assist in buying a quality product at a competitive price.

DUAL SOURCING

Senator GLENN. In General Skantze's prepared statement, he indicated that dual sourcing is an excellent technique for reducing program risk and production costs in selected situations, but it is not the panacea that current legislative proposals would lead one to believe. I also read yesterday where the Navy has issued an order directing that all new weapons systems will have two sources. There seems to be a lack of agreement here. I would appreciate your comments on the value of dual sourcing, both the leader-leader approach and the leader-follower approach.

General BABERS. Dual sourcing, as addressed here, pertains to the front-end portion of weapon system's life cycle and therefore is not an issue in which DLA is normally involved. From an overall logistics point of view, dual sourcing provides benefits in the spare parts arena by encouraging an expanded industrial base and by providing a greater opportunity for achieving competition in the procurement of spare parts.

DLA does not use the "dual sourcing" authority in the sense of "leader-leader" or "leader-follower" type procurement, because we are not in the business of developing new systems or items. We do however, have defacto dual sourcing for a limited number of items in order to maintain an adequate production base for potential mobilization needs. In these instances, we received the benefits of reduced program risk in the event one of the contractors fails. We also maintain competition in commodities that might otherwise become sole source if we didn't have multiple source contracts. We're strengthening our production analysis function to identify more situations where this technique should be applied. There are obviously situations where dual sourcing doesn't make sense in the production stage of a weapons system because the quantities involved won't economically sustain additional production facilities.

QUESTIONS SUBMITTED BY SENATOR SAM NUNN

MILESTONE AUTHORIZATIONS

Senator **NUNN**. I would be interested in your thoughts on alternative methods Congress might choose for authorizing major weapons systems. As you know, under the present process, Congress reviews each of the major weapons systems on an annual basis as part of the budget submission.

Some have suggested as an alternative that Congress revise its authorization process and authorize milestones for a system. At each milestone, the Department would provide a cost and performance baseline that would carry the program to the next milestone. If Congress authorizes the program milestone, the defense manager would be free to continue the program unless costs or performance deviate (by some preset percentage) from the baseline provided at the time of the authorization, until the system's next natural milestone. If cost or performance deviates from the baseline, Congress would review the program in the normal oversight manner.

Would it be feasible to move to a milestone authorization based on this outline?

General **SKANTZE**. We agree in concept with establishing authorizations based upon the Defense Systems Acquisition Review Council (DSARC) milestones. The proposal promotes more stable acquisition planning and is a step toward promoting program efficiencies and economies rather than the annual perturbations. Of course, the timely approval of appropriation must butress the concept if we are to truly benefit from such a process. We have several concerns, however, which must be addressed before such a concept could be made to work.

a. If a program is authorized at a major DSARC milestone, the annual (or biennial) appropriations debate would still subject the program to fiscal adjustments.

b. If a DSARC milestone occurs out of cycle with the congressional budgetary process, there appears to be no provision to authorize and appropriate funds concurrent with the DSARC decision.

c. Lastly, the time periods between major weapon program acquisition milestones are normally more than two years. Provisions are needed to allow DOD to contract and expend funds over the expected period versus the current two or three year limitation.

Senator **NUNN**. If such an authorization process were feasible, what milestone should Congress focus on?

General **SKANTZE**. We believe that DSARC milestones II and III are prime candidates for consideration for this concept. Milestone II is the point in the program where we start full scale development. Milestone III is the production decision. The phases after these critical milestones are where the major portion of the dollars are expended and where the fruits of our earlier acquisition strategies start to pay off. If we achieve stability during these phases, all our earlier planning should yield significant cost savings.

Senator **NUNN**. What would be the impact on the Department's planning and management on major systems if Congress decided to authorize systems on this basis?

General **SKANTZE**. It is not clear at this time what the impact to the Air Force planning and management of major weapon systems would be if we indeed went with such a concept. Our initial evaluation is that it would be minimal. Minor changes in policy would be required, but our policy is always under review. We believe that this area would require some detailed study to determine the overall impact to our acquisition process.

Senator **NUNN**. Are the management tools in place to implement such a process?

General **SKANTZE**. The basic tools to manage a program on this basis are in place. We have our baselining concept, cost reporting requirements at both the contractor and congressional level, and we have our program planning and control process that could accommodate this policy change.

Senator **NUNN**. What new management tools would need to be developed in order to proceed to milestone authorizations?

General **SKANTZE**. We would have to develop minor modifications to the basic tools discussed above to reflect the precise wording and intent of Congress when the legislation is actually passed.

Navy Response. We agree that some alternative is needed to the annual review by Congress of our major systems and we strongly support the biennial budget submission as such a means. We believe our current program and budget review is superior to the milestone authorization plan because it enables us to consider the balance of all programs in the fulfillment of a warfare mission and the maritime strategy. If directed to implement milestone authorizations, new budget and financial management procedures to accommodate multiple year funding would be needed. It may prove to be extremely difficult to match milestones to fiscal years.

SIMPLIFICATION OF PROCUREMENT PROCEDURES

Senator **Nunn.** Many commentators have indicated that the military could obtain the goods and services it needs without the need for the extensive rules, regulations and paperwork associated with the current acquisition system.

Would it be desirable to legislatively establish a pilot program that would permit the waiver of the application of many, if not most, of the laws affecting defense procurement?

If such a program were to be established, are there any laws or regulations that your service does not believe should be allowed to be waived by statute in such a pilot program?

If such a pilot program were desirable, what systems, or types of programs, should be considered for inclusion in any such pilot program?

How could such a pilot program be established?

General **Skantze.** We are always looking for ways to improve the acquisition of our weapons systems and have been studying the process for some time. Should these studies identify techniques that require testing, we will develop "pilot" programs to evaluate them. We expect to complete this work in the spring and will identify any "pilot" programs at that time.

In a broader sense, we have identified a preliminary list of procurement reforms, such as raising the dollar threshold for synopsizing procurements, elimination of as many redundant reports as possible, establishing mandatory warranty application only for major defense acquisition programs, and eliminating the "stay" provision for a bid protest after award. If implemented these can simplify our procurement process. You have separately offered to have our staffs explore these ideas. I welcome your offer and look forward to pursuing these ideas with your staff.

Navy Response. The Navy supports initiatives simplifying procurement procedures. For example, we endorse the proposed legislation "To amend the Office of Federal Procurement Policy Act to authorize tests of innovative procurement methods and procedures." Specifically, we view the proposed legislation for testing simplified small purchases and paperless procurement system as a move in the right direction, leading to additional improvement initiatives. Additional pilot programs waiving laws affecting the acquisition process should be considered and tested as appropriate.

Any decision as to which system or types of programs to be included in any test program or which laws and regulations need to be waived, should be made by the Service Secretary on a case by case basis. The establishment of any pilot program could result from legislative or DOD action.

"WHITE" VERSUS "BLACK" WORLD PROGRAMS

Senator **Nunn.** Many cite problems in the so-called "black" world as having a more rapid development schedule at less cost than programs open to public inspection.

What laws, rules, or regulations are waived, or are generally not applicable to the black world, that are applicable in the white world?

What rules or procedures, if any, differentiate the black programs from the white?

Based on your experience, do you believe the black programs have shorter development times than the white programs? If so, why? Does this also lead to reduced cost?

While some suggest that the black world programs are more efficient there are many who fear that the proliferation of rules and regulations in the white acquisition system may encourage defense agencies, program managers, and some contractors, to go or stay "black" to protect themselves from the rigors of oversight. What reviews and efforts does and will your Service take to ensure that the cloak of secrecy is not used unnecessarily to keep programs out of the public view?

General **Skantze.** Because there are no provisions in the laws for waivers based on program nature, we do not waive any laws on our "black" programs.

In general, however, to meet the program objectives, those regulations not founded in law are considered for a waiver on a case-by-case basis. The program objectives are usually driven by a schedule—to field perishable technology as rapidly as possible—and not cost. Because the program objectives emphasize schedule and because, as outlined below, we expedite virtually every aspect of the acquisition process of "black" programs, these programs do tend to have shorter development cycles than "white" programs. And, while there is not a one-for-one correlation between acquisition time and acquisition cost, we believe we can save money by doing things faster.

The main advantage of our approach to "black" program management lies in the expedited manner we approach everything. Thus, these programs have small teams of high caliber, hand picked, experienced people dedicated full time to the program. These people have more management authority and ready access to our senior leaders. Staff review is expedited because fewer people have access to the program and the necessary coordination is obtained very quickly. With ready access to senior leaders, decisions are also expedited.

Since this approach fundamentally requires experienced people and there are only a limited number of "small experienced teams" we can draw together, we cannot apply these techniques across the board.

The decision to initiate a "black" program and maintain it in the "black" world is not a one-time decision. We continually reassess the need for maintaining "black" programs and occasionally a program, such as the SR-71 or U-2, will turn "white". These decisions are made by the same senior leaders who review "white" programs. Thus, there is a continuity and check and balance built into both the initial decision and the review process to ensure "black" programs truly need the security restrictions imposed.

Navy Response. The Navy subjects both "White" and "Black" programs to all laws, regulations and rules. Additionally, "Black" programs are the subject of special oversight by senior Navy officials for all aspects including budget, technical, programmatic, and contracting. This review also includes the applicability of the "Black" classification to each program. The basic acquisition philosophies of SECNAVINST 4210, 6 e.g. fixed price contracts in FSED, increased contractor investment in tooling and test equipment costs, and multiple sources throughout development and production, are being applied to "Black" programs.

The same types of business approvals are required for these programs at the same management level as for "White" programs. The same lower level reviews, however, are not performed since these personnel are not properly cleared. This leads to shorter overall review time. No significant difference is seen between the two types of programs for schedule or cost.

The Competition in Contracting Act takes into account an exception to full and open competition in cases that would violate security requirements. The Small Business Act and the Office of Federal Procurement Policy Act also provide an exception to the requirement for synopsis of proposed procurements in the Commerce Business Daily, if the notice would compromise the national security. Nevertheless, all possible actions are taken by the Navy to promote competition and to publicize pending requirements among interested firms having the appropriate security clearances.

FAVORABLE USE OF INDEPENDENT COST ESTIMATES

Senator **Nunn**. In both the fiscal year 1985 and 1986 Defense Authorization bills, we have asked for reports on the Department's use of independent cost estimates in planning, budgeting, and selection of major weapons systems. Your statement indicates very favorable AFSC use of these estimates. Is your experience typical within the Air Force?

General **Skantze**. Yes, I would say that the Air Force Systems Command's experience with independent cost estimates, that is our Independent Cost Analyses (ICAs), is typical of the entire Air Force. Because of our development and procurement responsibilities for Air Force weapon and support programs, the Air Force Systems Command serves as the lead command for the vast majority of the Air Force's ICAs; however, there are ICAs required on major modifications and retrofit programs for which the Air Force Logistics Command is given primary responsibility. In addition, the Air Force Communications Command has led ICAs on its Inter-Service/Agency Automated Message Processing Exchange (I-S/A AMPE) program. The ICA has proved to be a valuable test of reasonableness in all instances and assisted in the system decision and PPBS processes.

Senator **Nunn**. Under what circumstances can independent cost estimates be most valuable to the services?

General **Skantze**. I believe the Independent Cost Analyses that are accomplished in support of the system decision process are the most valuable—in particular those that are developed in support of Milestone I and II Air Force System Acquisition Review Council (AFSARC) and Defense System Acquisition Review Council (DSARC) reviews when risk in varying degrees still exists and the system configuration is yet evolving. It is at these points that the test of reasonableness the ICA provides is most beneficial. As I stated in my testimony, the independent estimate, by the challenge it offers to the program estimate, encourages the realism that results from an independent review. It forces us to clarify program content, schedule, and management planning. This occurs because in arriving at its cost estimate, the team of independent analysts must examine and understand every aspect of the program. This rigorous, unbiased examination serves as a catalyst to everyone involved with a program. It causes reexamination, correction, and inclusion of things, that may have been previously overlooked. As a result of the process, we feel there is a tremendous benefit to program management from the independent review, as well as the cost estimating outcome.

Senator **Nunn**. Would you explain the primary difference between independent cost analyses (ICA) and independent cost estimates (ICE)? When are each most likely to be used, and when is it not appropriate to use either or both of these budgeting tools?

General **Skantze**. The Air Force uses the term Independent Cost Analyses (ICAs) to refer to those independent estimating efforts accomplished in support of the system decision process, i.e., AFSARC and DSARC major milestone reviews, and also the Defense Resources Board (DRB) for its deliberations on budget requirements. In both cases the ICA is used to test the reasonableness of the program office estimate. Basically, the ICA has two major components. First, is the independent estimate that is normally developed by a comptroller-led team, independent of program management influence and control. Second, is the comparison and reconciliation of variances between the independent and program estimates that must be accomplished. I consider the reconciliation to be equal in importance with the independent estimate itself in assuring the validity of the program office estimate.

The term Independent Cost Estimate (ICE) is used formally in the Air Force to connote any estimate prepared by an independent team that, as I have stated, is not under the control of the program office. It may be accomplished for any number of reasons, such as the inability of a program office to prepared its own estimate. In this case, an independent estimate is prepared and then adopted in whole or in part as the official program office estimate. An ICE may also result from management's desire to estimate something for which a program office does not currently exist, such as a theoretical system or proposed project. The ICE in all probability will serve some decision-making purposes, but it is a term used for estimating activity beyond the rather well-defined and standardized AFSARC/DSARC and DRB requirements which call for a challenge to an existing program office estimate.

SIMPLIFICATION OF PROCUREMENT PROCEDURES

Senator **Nunn**. Many commentators have indicated that the military could obtain the goods and services it needs without the need for the extensive rules, regulations and paperwork associated with the current acquisition system.

Would it be desirable to legislatively establish a pilot program that would permit the waiver of the application of many, if not most, of the laws affecting defense procurement?

If such a program were to be established, are there any laws or regulations that your Service does not believe should be allowed to be waived by statute in such a pilot program?

If such a pilot program were desirable, what systems, or types of programs, should be considered for inclusion in any such pilot program?

How could such a pilot program be established?

General **Babers**. A program that would provide for uniform application of the various statutory dollars thresholds only to acquisitions over $25,000 would be desirable. If these thresholds cannot be rationalized, as applicable, to small purchases, waiver of the application of these thresholds should be provided.

Unless the rationale for application of the various dollars thresholds applicable to small purchases can be provided, there are no laws or regulations that we believe should not be allowed to be waived for a pilot program. The specific statutory provisions that should be considered for waiver are provided in Appendix A of the Final Report on Simplification of Small Purchases prepared by Task Group No. 5 of the Executive Committee on Federal Procurement Reforms under Executive Order

12352 and by letter dated 4 December 1985 forwarded by the Director, Office of Management and Budget to Senator William Roth, Chairman, Senate Committee on Government Affairs and Representative Jack Brooks, Chairman, House Committee on Government Operations.

Appendix A to the Task Group No. 5 report was provided in DLA's Inserts for the Record to the testimony given on 29 October 1985 to the Senate Defense Acquisition Policy Subcommittee of the Committee on Armed Services hearings (Transcript Page No. 91, Line No. 7, Insert No. 10).

The small purchase program representing purchases of supplies and nonpersonal services valued at $25,000 or less should be include in such a pilot program. Approximately 97.6 percent of the total number of actions accomplished by DLA procuring activities in FY 1985 were small purchases. If waiver of the application of many, if not most, of the statutory requirements affecting small purchases were permitted, the small purchase process would become simpler, less administratively burdensome, less time consuming, and a smarter way to do business.

DOD should be granted the authority to initiate a pilot program permitting waiver of application of many, if not most, of the laws affecting defense small purchase procurements under its own established guidelines. Recommend that any resulting pilot program be established for a minimum of three years. This would provide for the program to be in effect through the procurement cycle from preaward through the postaward phase.

"WHITE" VERSUS "BLACK" WORLD PROGRAM

Senator **Nunn**. Many cite programs in the so-called "black" world as having a more rapid development schedule at less cost than programs open to public inspection.

What laws, rules, or regulations are waived, or are generally not applicable to the black world, that *are* applicable in the white world?

What rules or procedures, if any, differentiate the black programs from the white?

Based on your experience, do you believe that black programs have shorter development times than the white programs? If so, why? Does this also lead to reduced cost?

While some suggest that the black world programs are more efficient there are many who fear that the proliferation of rules and regulations in the white acquisition system may encourage defense agencies, program managers, and some contractors, to go or stay "black" to protect themselves from the rigors of oversight. What reviews and efforts does and will your service take to ensure that the cloak of secrecy is not used unnecessarily to keep programs out of the public view?

General **Babers**. With respect to the policies and procedures pertaining to certain classified programs, I defer to my service colleagues who may be in a better position to address these issues.

We have taken steps to assist in insuring that the security system is not abused. As part of the Department of Defense's efforts to tighten security procedures, we have reduced the number of security clearances in DLA by over 29 percent. We are also beginning an Agency-wide program to review our overall security posture.

MILESTONE AUTHORIZATIONS

Senator **Nunn**. I would be interested in your thoughts on alternative methods Congress might choose for authorizing major weapons systems. As you know, under the present process, Congress reviews each of the major weapons systems on an annual basis as part of the budget submission.

Some have suggested as an alternative that Congress revise its authorization process and authorize milestones for a system. At each milestone, the Department would provide a cost and performance baseline that would carry the program to the next milestone. If Congress authorizes the program milestone, the defense manager would be free to continue the program unless costs or performance deviate (by some present percentage) from the baseline provided at the time of the authorization, until the system's next natural milestone. If cost or performance deviates from the baseline, Congress would review the program in the normal oversight manner.

Would it be feasible to move to a milestone authorization based on this outline? If such an authorization process were feasible, what milestones should Congress focus on? What would be the impact on the Department's planning and management of major systems if Congress decided to authorize systems on this basis? Are the management tools in place to implement such a process today? What new management tools would need to be developed in order to proceed to milestone authorizations?

General **Babers**. The Defense Logistics Agency does not purchase major weapons systems. Therefore, we do not believe it is appropriate for us to respond to this question.

(Subsequent to the hearing the following letter was received from J.R. Sculley, Assistant Secretary of the Army. The questions from members of the committee with answers supplied follow:)

Department of the Army,
Office of the Assistant Secretary,
Washington, DC, January 15, 1986.

Hon. Carl Levin,
Ranking Member, Subcommittee on Defense Acquisition Policy, Armed Services Committee, U.S. Senate, Washington, DC.

Dear Senator Levin: Reference your letter of November 22, 1985 to Secretary Marsh with questions from committee members. Army responses to the questions are attached.

We appreciate the opportunity to provide comments for the oversight hearings on acquisition legislation, and would be happy to discuss our comments with the subcommittee and staff.

Sincerely,

J.R. Sculley,
Assistant Secretary of the Army
(Research, Development and Acquisition).

Enclosures.

STATUTORY REVISIONS

Senator **Quayle**. List for us any other problems with statute not already covered in this hearing that the subcommittee should be looking at; specifically what should be considered for repeal or modification and why.

Army Response. While the witnesses at the hearings have covered most of the legislative concerns of the Army, there are some additional problem areas that deserve mention.

The Paperwork Reduction Act and the Regulatory Flexibility Act both require publication for public comment in the Federal Register of new or changed procurement regulations. The necessity to publish notices in the Federal Register impedes the timely implementation of new policy, some of which is mandated by legislation, and procurement regulations should be exempt from these two Acts.

Recent legislation does not contain the long-standing exemption from synopsizing purchases in the Commerce Business Daily by contracting activities outside the U.S. The requirements to synopsize in such a case is impracticable and adds time and cost with no benefit.

The requirement for large businesses to develop small business subcontracting plans should be modified. Currently, a subcontracting plan with goals must be negotiated for most prime contacts over $500,000. A better way of accomplishing this would be for major contractors to develop annual plant-wide plans. This would replace multiple individual negotiations with a single negotiation that can consider the totality of a contractor's work for a year.

Conflict between the Service Contract and Davis-Bacon Acts in definitions of work and classification of laborers causes confusion over how to classify workers and which wage rates to apply and creates double standards when contracting for the same type of work.

The requirement for use of U.S. flag commercial carriers creates a constraint on transportation scheduling and could delay deliveries and increase costs.

The Appropriation Act provision that prohibits DOD from requiring small businesses to demonstrate they have an accepted commercial item inhibits our ability to buy and rely upon items proven in the commercial market place.

The Brooks Act is now unnecessarily restrictive and has outlived its usefulness with passage of CICA which requires reviews of all procurements when less than full and open competition is expected, including ADP.

Legislation covering military construction reduces flexibility of DOD in using military construction funds, and can adversely impact on the quality of life for soldiers and our ability to support new weapons systems. Congress should periodically review threshold for minor construction and evaluate requirements for advance notification.

In the area of taxes, Congress should examine the current application of Federal excise taxes imposed on contractors selling various items to the DOD. This artificially inflates the size of the DOD budget and cost of projects while only transferring Government funds from one account to another.

The Army recognizes and accepts the need for reform in the acquisition process. Many of the provisions of recent legislation, especially in the areas of competition and spare parts, were already covered by OSD or Army initiatives prior to becoming law. The concern the Army has is that the cumulative impact of so many new statutory provisions is to create unnecessary turbulence and complexity in the procurement system.

Stability and simplification of the procurement process is what is now called for.

GENERAL AND ADMINISTRATIVE EXPENSES INCLUDED IN PROFIT CALCULATIONS

Senator LEVIN. Could you support a change in DOD policy which excludes G&A from the markup base for your Service?

ARMY RESPONSE. Profit as a part of a price awarded in negotiated DOD contracts is generally proportional to a contractor's risk, investment and costs. General and Administrative cost (G&A), therefore, is not different from other cost elements used to calculate profit: the greater the amount claimed/allowed, the greater the profit—in absolute dollars, not percentages. Percent ranges for each cost element are established in Defense FAR Supplement; the exact percent within the range, however, represents the contracting officer's consideration of a contractor's effort.

G&A costs traditionally include the contractor's top management, financial services; legal; marketing/sales; independent research and development/bidding and proposal expense; corporate and corporate group allocations (management, stockholder and financial services, taxes, legal, etc.). The G&A expenses of the business unit itself are those which are necessary for doing business, and which promote the existence of a contractor that is a benefit to the Govenment.

Removal of corporate and/or groups allocations is a possible consideration inasmuch as the corporate functions performed would be a necessity regardless of government business. The lack of standardization among contractor accounting practices makes difficult such an approach. A more tenable approach would be to enlarge the weight range for profit consideration at the low end, thus allowing the contracting officer more room for consideration of the contribution of G&A to the overall effort of the program.

Senator LEVIN. If you agree with such a change, would such an action require legislation or could it be done administratively?

ARMY RESPONSE. The latter would require only a change to the DFARS.

AGENCY PURCHASING OFFICERS' MORALE

Senator LEVIN. In a recent interview, one of the OSD acquisition deputies stated that the morale of the acquisition work force had "sunk so low they don't talk to their relatives about it". Do you share the view of the morale of the Department's and your service's acquisition work force?

ARMY RESPONSE. I have no specific knowledge of the statement to which you refer, nor the context in which it was made. I am however concerned about the morale of the acquisition work force.

Senator LEVIN. Don't events such as the Navy Secretary's precipitous action to fire the three officials at the Miramar Naval Air Station contribute to the work force's fear of either making a mistake or overpaying for some parts?

ARMY RESPONSE. Our people truly want to do a good job and recognize their responsibility to the taxpayer. While they are concerned about firings, I believe they are equally or more concerned with the public's image of Federal employees and their own ability to keep up with current revisions to regulations and procedures.

Senator LEVIN. What actions has your service taken to enhance the prefessionalism of the work force?

ARMY RESPONSE. In conjunction with the other services, the Army has requested that the Office of Personnel Management take certain actions to enhance the professionalism of the work force. These actions include designation of procurement as a professional rather than administrative career field; establishment of a positive college degree requirement for entry into the career field; and relief from the Government Employees Training Act to allow us to send outstanding employees for advanced degrees.

In coordination with the other services, we have also developed and recommended to OSD a required set of experience prerequisites and training requirements for specific job functions in procurement. Army has developed and submitted to OSD a separate budget for mandatory procurement training and, as part of a DOD Task Group, has initiated action to establish centralized (OSD) funding for mandatory training.

Army is continually reviewing the training requirements and the existing training/education base and is developing recommendations to enhance the capability of the training/education base to peform its mission. Together with the other services we have initiated actions to have OSD ensure that all DOD schools are adequately funded and staffed.

In coordination with the Office of Personnel Management, we are exploring the use of selective and quality ranking factors for filling intermediate and senior level jobs.

We have developed and implemented a program to send both military and civilian employees to Training with Industry for approximately a one year period and are sending outstanding civilians to senior level schools. An Executive Training Program (Logistics Acquisition Management Program (LOGAMP) has been implemented which emphasizes cross training and development in the acquisition disciplines.

Additionally, non-supervisory GS/GM 14 and 15 contracting officer positions are being developed and implemented for selected major weapon system.

Finally, we are providing recognition of the procurement personnel by revitalizing Army and DOD awards programs and are developing and instituting additional awards to ensure proper recognition of outstanding performance.

PENALTIES FOR CONTRACTORS

Senator LEVIN. Included in the FY86 DOD conference bill are a number of significant penalties that will be imposed on defense contractors for submitting false claims, and overcharging for work, for example. Do you believe these penalties will act, as an effective deterrent to fraud for contractors doing business with the Pentagon?

ARMY RESPONSE. Yes, the criminal and civil sanctions included in this bill will significantly enhance the sanctions that can be imposed upon contractors who submit false claims or otherwise overcharge the Government. The severity of these increased sanctions, when properly enforced, will effectively deter Defense contractors from future fraudulent practices.

Senator LEVIN. Should these penalties be applicable to any contractor doing business with the Federal Government, not just DOD?

ARMY RESPONSE. The problem of procurement fraud is certainly not limited to the Department of Defense and these sanctions should be equally effective in deterring fraud directed against any Federal department or agency.

Senator LEVIN. Are these sanctions enough of a deterrent for DOD contractors?

ARMY RESPONSE. These sanctions, in addition to those already in existence, are adequate if properly enforced to effectively deter contractor fraud.

COMPETITION

Senator LEVIN. One of the goals of the 1984 legislation was to open up the Federal procurement process to new players, particularly small minority businesses. Have you seen an increase in the number of new competitors for many of your services purchases? Is your service getting a better deal for its dollar because of this new competition?

ARMY RESPONSE. There has been a notable increase in the number of companies, both large and small business, expressing an interest in competing for Army purchases since implementation of the Competition in Contracting Act (CICA) of 1984 on 1 April 1985. Expanded requirements for the synopsis of proposed procurements in the Commerce Business Daily and the requirements for full and open competition imposed by the CICA have contributed to many new potential sources for Army items based on comments made by Army Major Commands. While there are no statistics available regarding the number of new competitors on Army purchases, the increases in Army's competition rate from 42.3% in FY 84 to 46.9% in FY 85 indicates that a significant number of new companies competed for Army contracts.

The Army's Competition Advocates (240 total) are having discussions with numerous new potential sources. The Army's Competition Advocate General has met with representatives from over 80 companies to discuss their interest in becoming new competitors on Army procurements, many involving sole source items.

The benefits of competition are clear. The Army has experienced "good news" in competitive procurements. An example:

The FY 84 Hellfire Missile procurement was awarded competitively and resulted in a savings of $20.5M over the sole source projection for FY 85, and additional savings of $6–100M projected through FY 91. Breakout of launcher and container components are also expected to result in savings of over $80M.

COMPETITION VERSUS QUALITY

Senator **Levin**. In Dr. Wade's statement, he noted the need to ensure that the Department builds or maintains high quality into the systems and parts that you purchase. Do you see any diminution in your service's ability to obtain quality products and services while at the same time undertaking an aggressive competitive program?

Army Response. Prior to award of any contract, we have always required that a review and positive finding be made as to the contractor's ability to perform, including his ability to provide a quality product or service. With the increase of competition, particularly in terms of first-time successful contractors, there is a potential for an increase in awards to those who may not produce quality items. We are aware of this potential and are increasing our emphasis on quality assurance, as well as other indicators of a potential contractor's capability to perform, in our preaward determinations of responsibility. Therefore, we do not believe that the Army's ability to maintain the quality of the products and services purchased will be diminished.

WORK MEASUREMENT STANDARDS

Senator **Levin**. One of the issues which the Congress has been facing recently is the need to collect information on a contractor's work measurement goals and achievements.

Do you now routinely request this information from contractors?

Army Response. No, the Army does not routinely request such information. Generally, it is requested only from contractors that use work measurement standards to develop their proposals.

Senator **Levin**. If this information is made available to you, how is this information used by your service?

Army Response. The information is used to assess the productivity and efficiency of the contractor in the areas of direct costs for material and labor. Of particular interest is the trends over time of a contractor's variances from his standards.

Senator **Levin**. If this type of information collected from contractors was expanded, how would you take advantage of the additional information?

Army Response. The Army is currently participating in a major study of the potential use of work measurement data from contractors by project managers and others. This study, headed by the DODIG, will be completed in the summer of 1986.

REVOLVING DOOR

Senator **Levin**. You talked about the importance of a well-trained and motivated workforce. As you know, the debate is continuing in the Congress on an appropriate governmental policy for the "revolving door."

Do you think that individuals in the DOD acquisition workforce should be automatically precluded from going to work with a defense contractor solely because of the position that the individual holds within DOD?

Army Response. Postemployee restrictions on former DOD acquisition personnel should be limited to those necessary to avoid real or apparent conflicts of interest. However, an automatic bar on *any* employment with a defense contractor based solely on one's DOD position appears to be an unnecessarily broad restraint on the movement of talented and well-motivated individuals between industry and Government service.

Senator **Levin**. What do you believe an appropriate "revolving door" policy for contracting personnel in your service should be?

Army Response. It is questionable whether any further statutory postemployment restrictions, in addition to those already in force, really are necessary to protect the integrity of DOD procurement programs. However, if some additional restrictions should be deemed necessary to avoid negative public perceptions in this regard, the Army believes that a prohibition on employment with a particular defense contractor for one year after separation from Government service, where the former Government employee had substantial involvement with that contractor's activities during his or her last year in Government service, would certainly be adequate.

Senator **Levin**. Should this "revolving door" policy be applied only against DOD employees, or should it be applicable Government-wide?

Army Response. Any such restriction should be applicable Government-wide. Even if a particular agency does not have "revolving door" problems, a Government-wide policy would do it no harm—it merely would have no impact on the agency.

TRANSLATING LEGISLATION INTO IMPLEMENTATION

Senator **Levin.** In your statements, you indicated that the enactment of legislation is only the starting point for the implementation of changes within the procurement system. What would the normal flowchart and timetable be within your service for a legislative requirement to go from enactment in Washington to implementation at one of the buying centers?

Army Response. The normal process for implementation of new legislation in the DOD begins with the Defense Acquisition Regulation (DAR) Council. This Council is responsible for issuing and maintaining the primary procurement regulation within the DOD, the Defense Federal Acquisition Regulation Supplement (DFARS).

Upon receipt of legislation requiring implementation, the DAR Council will request one or more of its committees to prepare proposed changes to the DFARS. The committees are organized according to subject matter and are composed of subject matter experts from the Services, the Defense Logistics Agency and, if appropriate, the Defense Contract Audit Agency. The changes that must be made to the DFARS can be simple or complex depending on the legislation.

After the committees have prepared their recommended changes, they are considered by the DAR Council. It may be necessary to coordinate the proposed changes with the Civilian Agency Acquisition Council if the legislation impacts on the civilian agencies. It may also be necessary to involve the Office of Federal Procurement Policy.

When the DAR Council has approved the final proposed changes, they are published in the Federal Register for public comment as required by the Paperwork Reduction Act and the Regulatory Flexibility Act. Further, if the new Defense policy will require contractors to provide data or information, OMB clearance is required by the Paperwork Reduction Act.

Depending upon the substance of the public comments, the case may have to be referred back to the committees for further work. Eventually, the case will be approved by the DAR Council and the changes to the DFARS issued in a Defense Acquisition Circular. Generally, the Army will issue changes resulting from legislation through its own regulatory channels without waiting for a circular if the changes are not too voluminous.

Once the DAR Council has issued new policy, the Army must determine if further implementation is required. Generally, any further implementation would be of a procedural nature. That is, the establishing of review and approval levels, paperwork flow and so forth.

Implementation within the Army can be quite involved, depending upon the requirements of the legislation. For example, implementation of CICA required establishing Competition Advocates at various levels, developing Justification and Approval formats, establishing review and approval levels, etc. Often new legislation will require implementation outside procurement channels. CICA required implementation in requirements and technical communities, and the warranty legislation resulted in changes to supply and maintenance regulations and procedures and had impacts down to the lowest troop unit in the Army.

Another complicating factor is the increased reliance within the Army on the use of ADP to produce contractual documents. Any changes to the "boilerplate" then requires reprogramming of ADP systems which can be quite time consuming. The application of new policy is not delayed pending the reprogramming, but the new policy cannot be said to be fully implemented until it is fully institutionalized which includes insertion into standard ADP systems.

Fundamental changes such as CICA will also require training of thousands of procurement and other personnel.

There are no established timeframes within the Army for implementing new legislation. Generally speaking, the greatest amount of time is taken at the front end, with promulgation of DOD or Government-wide policy and procedure.

MANAGEMENT OF TECHNICAL DATA AND COMPUTER CAPABILITY

Senator **Bingaman.** Do you share my view that the management of the technical data, including indexing, storage and retrieval is as important to the Department as the ability to obtain that data in the first place? What actions are you taking to better manage the technical data that you now have and that will be obtained in the future?

Army Response. Management of technical data is certainly as important as our ability to acquire the data. If we do not have adequate tools and procedures to let us effectively use technical data, then there is really no sense in acquiring the data in the first place. In this vein, the Army is taking a variety of steps to better manage both the data we now have and that data that we will be obtaining.

Our primary effort to improve our technical data storage and retrieval capability is the acquisition of the Digital Storage and Retrieval Engineering Data System (DSREDS). DSREDS, which is a joint Army/Air Force acquisition, will provide a system that digitizes and stores the Army Materiel Command's (AMC) engineering drawing data base in digital format on an optical disk mass storage device. Implementation of DSREDS will improve our access to the drawing data base and will shorten the administrative lead time associated with putting a procurement package together. DSREDS will also provide an improved capability for drawing revision, thus improving our ability to maintain our technical data packages. DSREDS will also better support our future technical data acquisitions in that it provides for acceptance of data from the contractor in a digital format.

Coupling DSREDS' digital data acceptance capability with other Army actions to implement the Department of Defense Computer Aided Logistics Support (CALS) program will further enhance our capability to manage technical data that we receive in the future. Current Army actions to support CALS are focused through AMC's Technical Information Management System (TIMS), a program that will provide an overall architecture for location, storage, retrieval and use of all varieties of technical information.

The Army effort to improve management of technical data package information has AMC improving the policy and procedures that are used to determine what data will be bought, how the data acquisition program will be managed, and what the acceptance criteria for the technical data will be. In addition, AMC has an on-going effort to redesign the Technical Data/Configuration Management System, which is an automated technical data package indexing and maintenance system.

PREQUALIFICATION OF BIDDERS

Senator Dixon. What actions are you taking to reduce the use of prequalification requirements which were in existence on the effective date of the Defense Procurement Reform Act?

Army Response. All Army procurement actions are reviewed with respect to requirements of the Competition in Contracting Act (CICA), notwithstanding the "grandfather provision" of the Defense Procurement Reform Act. Any procurement action using other than Full and Open Competition is the subject of a complete Justification and Approval action incorporating the certifications, reviews, and approvals required by CICA.

Safety-of-flight requirements for aircraft and integrity-of-end-item concerns for missile systems have led to some use of "approved manufacturers' lists". The primary thrust of Army actions in this area, however, is toward critical review of "prequalification" techniques such as Qualified Producers/Products Lists and Source Control drawings with a view toward their reduction/elimination in use.

RELATIONSHIPS BETWEEN THE SERVICES AND SBA BREAKOUT PCR

Senator Dixon. Why do you believe that SBA is a competitor to the service in its efforts? What would you like to see the relationship be between SBA and your service's breakout and competition advocate functions?

Army Response. Though engaged in the same functions, the SBA Breakout Procurement Center Representatives (BOPCRs) have a different mission, report through different channels, and perform towards an objective different from that of our service personnel. The P.L. 98-577 requirement that the SBA BOPCRs report breakout cost avoidances attributable to their efforts establishes a direct confrontation between service functional personnel, in that they are also charged with an identical requirement. The methods and techniques of performing this measurement are only now being firmly established and segregating base data to facilitate separate reporting will require advance planning and negotiation.

SBA BOPCR reporting of breakout actions which is concurrent and consolidated with service reporting may remove much of anticipated competition. The requirement for separate reporting of cost avoidances will have to be worked out between SBA and each service. The Army fully intends to incorporate the SBA BOPCR into its ongoing performance of the DAR Supplement #6 Breakout Program, to whatever degree of cooperation can be established with SBA.

LEGISLATIVE IMPROVEMENTS TO PROCUREMENT

Senator **Glenn**. I think it is generally agreed that the 1984 procurement legislation was the most substantive change to procurement law since the Armed Services Procurement Act of 1947. In addition to your statements on modifications, I would be interested if you could tell us what part of the 1984 legislation has improved the DOD acquisition process the most, and why?

Army Response. The Competition in Contracting Act (CICA) provisions that place sealed bidding and competitive negotiation on a par for the first time is a definite improvement. Generally, it is too early to determine the overall impacts of the 1984 legislation.

PROGRAM MANAGEMENT

Senator **Glenn**. There has been concern expressed by many that acquisition reforms may have curbed the flexibility and authority of program managers. In testimony before this subcommittee last week, Dr. Wade stated that our flexibility to take advantage of research and technology may be inhibited by statutory reform. Do you believe that the 1984 legislation has reduced the effectiveness of program managers?

Army Response. The transition period associated with implementation of the 1984 reform legislation has caused confusion and turbulence througout acquisition communit including the Project Management Offices. We do not believe, however, that when the dust settles this legislation will materially impact on the Project Manager's ability to take advantage of innovative research and technology.

MANAGEMENT OF RESEARCH AND DEVELOPMENT PROGRAMS

Senator **Glenn**. Many of these same concerns have been expressed about our ability to effectively manage research and development programs. My major concern is the potential impact on several research and development programs just getting started, such as SDI, Small ICBM, ATB and V-22.

Army Response. Substantial Army efforts are now expended to induce industry to invest their own resources, as well as their imagination, to explore the state-of-the-art and to strive for technical breakthroughs that have military application. As mature technology is critical to such new research and development programs such as SDI, any acquisition reforms that impact the quality or availability of that technology is of concern.

TECHNICAL DATA

Senator **Glenn**. During the hearing with Dr. Wade, I mentioned that I continue to be concerned about going too far in the area of technical data. The contention of many in industry is that the proposed implementing regulations do not reasonably balance the interests of the government and industry; that they favor government. I am also concerned about the disincentives to industry to conduct private research and development which is absolutely vital to our defense technical base. I would appreciate your views on this matter.

Army Response. Your concern in this area is understandable and shared by the Army. The issue of how to best satisfy our requirement to increase competition and at the same time not stifle private sector investment in research and development is a challenge for both us and industry. We believe that sufficient latitude is provided to allow us to meet this challenge.

Industry must meet us half-way on this issue and realize that we are serious in our commitment to broaden the scope of competition. This does not mean we will not reimburse industry for their legitimate and reasonable research and development investments. It does mean that the Army will challenge industry claims of proprietary data and what is a fair and reasonable price for the purchase of rights in data.

QUALITY IN THE ACQUISITION PROCESS

Senator **Glenn**. In Dr. Wade's testimony, he stated that competition is "too frequently based on price," and an "award to the low bidder" mentality. He indicated that DOD plans to move away from defining equipment requirements in terms of minimally acceptable terms to the system whereby the best quality equipment at an acceptable price is the recognized objective. I strongly support this objective, but was surprised that this quality issue was not addressed in any depth in any of the statements. I would appreciate your comments on cost versus quality as it relates to the current procurement regulations.

Army Response. The Federal Acquisition Regulation clearly recognizes that awarding contracts on price alone is not always good business and states that "The award of a contract to a supplier based on lowest evaluated price alone can be false economy if there is subsequent default, late deliveries, or other unsatisfactory performance resulting in additional contractual or administrative costs". Contracting for supplies can be performed through either sealed bidding, or through negotiation. When the selection of a successful bidder will be made on price alone, sealed bidding may be the most effective means of contracting. However, when factors other than price will be evaluated, negotiation is the proper method to use. The important thing to remember is that we must tell the contractor what we think is important.

While solicitations inform offerors of the minimum requirements, evaluation criteria such as quality and performance characteristics, called out in the solicitation can encourage contractors to submit proposals which will go beyond the minimum requirements specified. Once the contractor understands quality is equally as important as price, we should begin to see proposals that are structured on a best value basis. While weighted factors are not new to source selection, there has been increased emphasis to give quality and performance equal weight to price.

DUAL SOURCING

Senator Glenn. In General Skantze's prepared statement, he indicated that dual sourcing is an excellent technique for reducing program risk and production costs in selected situations, but it is not the panacea that current legislative proposals would lead one to believe. I also read yesterday where the Navy has issued an order directing that all weapons systems will have two sources. There seems to be a lack of agreement here. I would appreciate your comments on the value of dual sourcing, both the leader-leader approach and the leader-follower approach.

Army Response. Dual Sourcing requires the use of innovative contracting techniques to develop and sustain a truly competitive environment. There are any number of arrangements which can be used dependent on the unique circumstances of the particular acquisition. All have benefits and drawbacks. For example, the leader-leader concept allows for simultaneous dual development causing increased development costs and possibly increased logistics costs; the benefit of the leader-leader concept is competition early in the life cycle. The leader-follower arrangement is just the opposite. Any number of variations of these two basic arrangements can be used to try to maximize the benefits of both. For dual sourcing to result in true benefits, the quantity to be procured must be sufficient to offset the investment cost associated with dual development, where applicable, increased facilitization costs and reduced efficiencies attributed to lower production rates.

SIMPLIFICATION OF PROCUREMENT PROCEDURES

Senator Nunn. Would it be desirable to legislatively establish a pilot program that would permit the waiver of the application of many, if not most, of the laws affecting defense procurements? If such a program were to be established, are there any laws or regulations that your service does not believe should be allowed to be waived by statute in such a pilot program? If such a pilot program were desirable, what systems, or types of programs, should be considered for inclusion in any such pilot program? How could such a pilot program be established?

Army Response. Such a program would be desirable from the standpoint of substantiating the efficiencies to be accrued in the absence of legislative and regulatory constraints. There are many laws and regulations which we would not desire to waive since they represent sound business practices which we would follow in any case or provide the Government benefits we otherwise could not obtain. However, in order to allow maximum flexibility within the Department to surface all areas where benefits can be gained, no statutory limitation on the waiver authority should be imposed.

The pilot could be approached one of two ways. The first method would be to establish a procurement simplification program to cover purchases under a certain dollar threshold similar to the DOD proposed Simplification Program for buys between $25,000 and $5 million. This type of pilot would be the easiest to implement. The second method would be to establish and control a pilot consisting of a mix of selected production and development systems. In this case, the pilot would cover the major system and subsystems for the selected programs, as well as support services and parts including such parts as may be common to other weapons systems. Establishment of this type pilot would require special controls. For the pilot to work, however, these controls should be as unburdensome as possible.

In either instance, it must be recognized that each law and regulation, for the most part, has or had an initial "positive intent;" thus during the pilot, it must also be recognized that such "positive intent" will be forgone.

"WHITE" VERSUS "BLACK" WORLD PROGRAM

Senator NUNN. Many cite programs in the so-called "black" world as having a more rapid development schedule at less cost than programs open to public inspection.

What laws, rules, or regulations are waived, or are generally not aplicable to the black world, that are applicable in the white world?

What rules or procedures, if any, differentiate the black programs from the white?

Based on your experience, do you believe the black programs have shorter development times than the white programs? If so, why? Does this also lead to reduced cost?

While some suggest that the black world programs are more efficient there are many who fear that the proliferation of rules and regulations in the white acquisition system may encourage defense agencies, program managers, and some contractors, to go or stay "black" to protect themselves from the rigors of oversight. What reviews and efforts does and will your service take to ensure that the cloak of secrecy is not used unnecessarily to keep programs out of the public view?

ARMY RESPONSE. In the Army the so-called "black" world programs have had a significant increase in formal managerial oversight for Special Access Programs (SAP's). Since September 1984, HQ DA has established an organization whose sole responsibility is to oversee all aspects of SAP's and to ensure compliance with existing regulations. Additional guidance on formation, administration and formal review of all Army SAP's has been instituted.

There are no waivers of statue normally associated with Army SAP's; however, deviations for security reasons can be authorized from normal white world requirements under the Federal Acquisition Regulation and Department of Defense Federal Acquisition Regulation Supplement.

Additionally, due to the emphasis on limiting access for security purposes, other policy procedures or requirements may also be waived such as: exemption from normal distribution of Selected Acquisition Reports (SAR's) and Cost/Schedule Control System Criteria (CS^{2}C) reports.

Having a program under special access caveats does not ensure any shortening of the development cycle. Because individual programs vary, one conclusion that can be drawn from past experiences is that greater developmental risks may be assumed in overlapping RDTE and initial production strategies. If the program is extremely successful in its developmental cycle, this forward lean may decrease the production milestone decisions by as much as two years. This, however, has proven to be the exception and not the rule.

The primary rationale for establishing Special Access Programs is to protect sensitve program information, and as such has some access constraints which have been viewed as preempting acquisition management requirements. DA has modified and published guidelines that require the same management process as white world systems although limited access to agencies (numbers of people cleared) will be enforced. DA has also imposed a thorough annual review by the Army leadership to determine the programs continuation as a Special Access (black) Program.

MILESTONE AUTHORIZATIONS

Senator NUNN. I would be interested in your thoughts on alternative methods Congress might choose for authorizing major weapons systems. As you know, under the present process, Congress reviews each of the major weapons systems on an annual basis as part of the budget submission.

Some have suggested as an alternative that Congress revise its authorization process and authorize milestones for system. At each milestone, the Department would provide a cost and performance baseline that would carry the program to the next milestone. If Congress authorizes the program milestone, the defense manager would be free to continue the program unless costs or performance deviate (by some preset percentage) from the baseline provided at the time of the authorization, until the system's next natural milestone. If cost or performance deviates from the baseline, Congress would review the program in the normal oversight manner.

Would it be feasible to move to a milestone authorization based on this outline? If such an authorization process were feasible, what milestones should Congress focus on? What would be the impact on the Department's planning and management of major systems if Congress decided to authorize systems on this basis? Are the management tools in place to implement such a process today? What new management tools would need to be developed in order to proceed to milestone authorizations?

ARMY RESPONSE. The system of annual congressional review of major weapons systems potentially creates program instability. A revision to this current methodology, such as congressional authorization at program milestones, could be beneficial by creating greater stability and cost control. The Army is implementing a procedure that emphasizes a baseline approach. The Program Management Control System (PMCS), provides the necessary management tools to support a congressional authorization at program milestones. PMCS requires the development of a cost-performance-schedule baseline. A document, the Program Directive (PD), is signed between Headquarters Department of the Army, the materiel developer and the user covering program execution. A major deviation from the Program Directive requires a decision for program change at the Department of Army. This Army program is fully compatible with the proposed modification to congressional authorization. The authorization process should be effective at each major milestone and subsequent major modification. At each major milestone (ASARC/DSARC) the Program Directive or baseline would be revised for the next acquisition phase. The thrust is to establish a set of basic system parameters and design for development, testing, and fielding of the baseline system. Major modifications would be put in a stand-alone line requiring separate justification and funding. Such a system would produce a greater degree of program stability and cost control allowing more systems to be put into the hands of our soldiers sooner and at a lower cost. Current Army management tools being implemented would allow execution of the new authorization approach provided OSD and Congress agree to the system baseline and funding levels.

[Whereupon, at 12:05 p.m., the subcommittee adjourned, subject to the call of the Chair.]

IMPLEMENTATION OF THE 1984 DEFENSE PROCUREMENT LEGISLATION

THURSDAY, NOVEMBER 7, 1985

U.S. Senate,
Committee on Armed Services,
Subcommittee on Defense Acquisition Policy,
Washington, DC.

The subcommittee met in open session pursuant to notice, at 10:03 a.m., in room SD-138, Dirksen Senate Office Building, Senator Dan Quayle (chairman) presiding.

Present: Senators Quayle, Goldwater. Levin, Bingaman, Dixon and Glenn.

Staff present: Alan R. Yuspeh, general counsel; Alan L. Chvotkin, counsel; Jonathan L. Etherton, professional staff member; and Marie Chaillet, staff assistant.

Also present: Bill Hunter, assistant to Senator Quayle; Alan Ptak, assistant to Senator Gramm; Francis J. Sullivan, assistant to Senator Stennis; Edward McGaffigan, Jr., assistant to Senator Bingaman; Charles C. Smith, assistant to Senator Dixon; and Milton D. Beach, assistant to Senator Glenn.

Also present: Bill Montalto, Small Business Committee.

OPENING STATEMENT BY SENATOR DAN QUAYLE, CHAIRMAN

Senator Quayle. The subcommittee will come to order.

Today we continue our preliminary assessment of the implementation of the 1984 defense procurement legislation with the first of two public witness hearings. We have invited representatives from four major trade associations to present the preliminary concerns of their members regarding recent changes to the defense acquisition process.

As I stated at the outset of these hearings, it is critical that this subcommittee exercise its oversight function. We have an unprecedented amount of new legislation over the past 2 years and more is surely on the way.

In the case of oversight of the 1984 legislation, it is important that we start now to examine issues that are surfacing as the law is being implemented. The earlier hearings in this series have already raised a number of problems and potential problems that we must closely monitor as the various implementing regulations go into effect and the impact of this new legislation is felt.

It is equally important that we have a clear assessment of the positive changes that have resulted from the enactment of this legislation, for it is clear that many of these fundamental reforms were long overdue.

Having heard from Government acquisition policymakers and professionals on these issues, we must now turn to the other major player in the acquisition process, the defense industry.

Today our four witnesses include:

Mr. John D. Rittenhouse, executive vice president, RCA Aerospace and Defense, representing the Electronic Industries Association.

Mr. Charles W. Stewart, president, Machinery and Allied Products Institute.

Mr. Karl Harr, president, Aerospace Industries Association.

Mr. Vico Henriques, president, Computer & Business Equipment Manufacturers Association.

[The opening statements of Senators Dixon and Glenn follow:]

Prepared Statement by Senator Alan Dixon

Mr. Chairman, this is our third oversight hearing of the Defense Acquisition Policy Subcommittee on the implementation of the 1984 defense procurement legislation. Our first two hearings consisted of testimony from the military services. We will now be hearing from representatives of industry.

Mr. Chairman, I look foward to hearing from these witnesses. I hope their testimony will continue to give us the type of information we need regarding the implementation of the legislation Congress passed last year. I intend to carefully monitor this entire process, because it is a matter of special interest to me.

Thank you, Mr. Chairman.

Prepared Statement by Senator John Glenn

Thank you, Mr. Chairman. I would also like to thank our witnesses for appearing today, and compliment them, and the companies they represent, for their forthright and constructive comments on the 1984 procurement legislation. Although there is no question that some changes are required in the way DOD does business, in our zeal to make these changes, we have to continually guard against going too far, too fast—to guard against doing serious damage to our defense industry that has through the years made a vital contribution to the defense readiness of this country.

When it comes to running a business efficiently, especially a large business like DOD, we need the continuous input from the business professionals like those represented here today. In fact it is essential that we work together if we are to achieve our mutual goal of a greatly improved acquisition system.

Senator **Quayle**. The first witness will be Mr. John Rittenhouse, executive vice president, RCA Aerospace and Defense, representing the Electronic Industries Association.

Mr. Rittenhouse, before you begin, I can tell you that your entire statement will be made a part of the record. Perhaps you might want to summarize and highlight the important points so that we can have time for questions and discussion.

STATEMENT OF JOHN D. RITTENHOUSE, EXECUTIVE VICE PRESIDENT, RCA AEROSPACE AND DEFENSE (REPRESENTING THE ELECTRONIC INDUSTRIES ASSOCIATION)

Mr. **Rittenhouse**. Thank you.

I am John Rittenhouse, executive vice president, RCA Aerospace and Defense, and I am pleased to appear here this morning on behalf of the Electronic Industries Association (EIA). The EIA is made up of some 500 electronics manufacturing firms, many of which provide products to the Department of Defense.

I thank the subcommittee for the opportunity to be heard on a subject that is so critical to the future of our Nation.

There is no question that there have been and still are problems in the way our Nation has acquired the products and systems needed for its defense.

The deficiencies that do exist in our defense procurement process have evolved over years and decades, and all of us—industry, the Department of Defense, the military services, and the Congress—have contributed to difficulties we are experiencing today.

For those problems to be eliminated—as they must be—all of us must work together, without fingerpointing or buck-passing. These hearings are a positive step in that direction.

To establish a framework for my remarks today, I would like to outline three fundamental premises that are given in discussions of defense system procurement.

In the context of these three fundamentals, I will then provide some specific recommendations, from a contractor's point of view, on what can be done to improve the procurement process. These suggestions concern the reorganization of DOD's acquisition organization, and ways in which we might add a positive dimension to acquisition methodology based on rewards for quality improvement.

The first fundamental premise is that the primary goal of everyone involved in the defense acquisition process—private industry, the military, the civilian defense establishment, and Congress alike—is to provide our servicemen and women in the field with high quality, reliable, affordable equipment, capable of meeting any threat to our national security.

I assure you that defense contractors do recognize the special trust and obligation that our work entails, an obligation that ultimately must transcend the profit motive.

The second premise is that, unlike most commercial industries, where the ability to cut cost and improve quality translates almost automatically into increased profit, defense is a cost-based business. Basically, that means that we have a different structure to earn profit—since profit is determined as a percentage of our cost.

As a result, in today's acquisition system, industry in many cases does not have enough motivation to reduce its costs on a contract. Indeed, in some flexibly priced contracts, there are a good many disincentives to cut costs. And even in competitively won, firm fixed-price contracts, the motivation is to be only slightly better than the competition.

There is no real long-term incentive to lower costs, particularly since we may be locked into those established lower rates in subsequent bids on follow-on contracts and other business.

The solution does not lie in more legislation regarding competition, but rather in the adoption and implementation of positive incentives to reduce costs and stimulate efficiency, some of which I will elaborate on later.

The third premise is that we have, over a period of years, decided that we cannot field a numerically superior force, so we must field a technologically superior reliable force structure.

In our haste to improve the acquisition process we have focused on competition as a means of ensuring the affordability of defense procurements. And, indeed, competition in many instances has been a powerful tool for lowering costs.

But competition alone will not endure meeting our objectives. Detailed and exquisite certification of rate structures may satisfy the need for accountability, but it does little to improve the quality of the product.

Ultimately, we must not only achieve cost reduction, but we must also achieve reliable equipment with technological superiority. Such a task will require a procurement organization that can deal with all the issues, and an incentive approach for industry which makes improved quality a never ending objective.

And so I would like to turn to the area of organization first.

Today's acquisition environment is indeed complex. In contrast with the scenario a few years ago—when a strong Government program manager was the central figure of procurement and administration authority—we now find diffused responsibility, amongst a variety of military and civilian implementation and monitoring agencies.

Today, a great many of the program decisions are made within the OSD and Congress, and a new power structure has emerged within the civilian secretariat.

In just the past 2 years, Congress has imposed major reforms on the procurement process, including the Competition in Contracting Act (CICA); warranties; and other procurement policy matters addressed in the Small Business and Federal Procurement Competition Enhancement Act of 1984.

Because of the breadth of the reforms and the speed at which they were enacted, DOD naturally has found it extremely difficult to implement the intent of these laws even in instances where Congress codified existing concepts.

Let's examine one such revision, perhaps the simplest of them all. On February 28, 1984, as one of its spare parts initiatives, DOD directed the services to provide under contracts for commercial parts that the price being charged to the Government, all other things being equal, is no more than the lowest price charged to the most favored commercial customer.

This was subsequently codified in brief and simple terms in Public Law 98-525 and Public Law 98-577 in October 1984. Congress adopted the simple, clean terms of the DOD directive.

DOD's implementation of this statute has yet to be accomplished. It took 9 months to effect what should have been a simple revision, and this was without public comment on the basis of public exigency.

The result was language so far afield from Congress' intent that OMB, in an unprecedented action, disapproved the regulation on the basis of its content rather than its form.

As a result of the burden placed on DOD, implementation of the law is lagging, and there is great disparity in interpretation between DOD and civilian agencies and among elements of DOD itself.

[Additional information follows:]

We believe that it is incumbent on Congress to insure uniform, concise and timely dissemination and implementation of legislative reforms.

Mr. Rittenhouse. As things currently stand, multisource management and hastily prepared directives result in a great deal of confusion for industry.

In another example, Secretary Weinberger authorized a new requirement for the certification of all overhead cost submissions, under penalty of perjury.

In the 6 months since that mandate was issued, we have seen the issuance of:

Two clarifications by DOD's legal counsel.

Two clarifications by the Deputy Under Secretary of Defense for Acquisition Management.

Two clarifications by the Chairman of the DAR Council.

A DAR Council issuance as a temporary regulation.

A revised temporary regulation.

And, no final regulation.

Each service and the Defense Contract Audit Agency (DCAA) were left to accomplish implementation in a wide variety of contradictory ways.

The resulting confusion in the field has created situations in which negotiations have stopped completely, and companies have seen their progress payments and final payments needlessly stopped.

Some proposals are being audited, others not, and many companies are unable to settle final overhead rates dating back 7 years.

Also adding to the confusion over responsibility and accountability is the split of authority between the contracting officer and the auditor.

That development is just one example, by the way, of another major problem in our defense procurement system—the growth in recent years, in terms of both size and power, of a diverse acquisition monitoring organization that is the second major group impacting on today's acquisition process.

DCAA, DCAS, GAO, the IGs, OSHA, EPA and the Department of Labor are only a few of the Government entities now involved in acquisition monitoring, in areas including allowable costs, overhead rates, pricing, quality, environmental concerns, worker health and safety, minority and small business subcontracting, and the list goes on and on.

We certainly recognize the need for oversight, but the demands of dealing with the flood of audits, investigations and reviews in our industry are consuming an ever-larger portion of our human and financial resources, and the cost of all this must be recovered in the prices contractors charge the Government.

As I indicated earlier, over the past 10 years a substantial measure of authority for Government acquisition has shifted to the Congress—the third major entity affecting the procurement process.

In 1975, four congressional committees were writing legislation involving defense issues, including procurement. Today more than 60 congressional committees and subcommittees find defense-related issues on their agendas.

For example, there have been legislative efforts by Congress to encourage wide use of work measurement standards throughout the defense industry. These efforts would only affect a small percentage of total product cost, and could easily be outweighed by additional administrative costs.

Although such measures are born from frustration with our industry, it seems more appropriate to charge an authoritative acquisition entity with the responsibility to implement corrective action, rather than invoke specific detail via the legislative route.

I can assure you that industry wants to assist Congress in its effort to reform the procurement process. But a fair, cost-efficient procurement system can exist only in a stable environment, and many of the recent efforts at reform have, in fact, contributed to increased instability in the system.

I have outlined just a few examples of such destabilizing factors in the areas of acquisition organization, acquisition monitoring, and congressional oversight.

I would urge Congress to refrain from taking any additional initiatives until these changes have been assimilated by the system, and I recommend that the Packard Commission, as it has come to be called, be given time to make a balanced, thoughtful and complete examination of the many complicated issues involved before any plan for procurement reform can be enacted.

I will follow my own advice; and then await the Packard Commission's assessment of just how the acquisition process should be specifically structured. But I do urge you to consider three elements that true reform of the process demands:

No. 1, a single well-defined procurement chain within the Department of Defense.

No. 2, a single well-defined monitoring and auditing authority.

No. 3, a single, well-defined structure for congressional inquiry and oversight.

In other words, please decide who is in charge.

Also, I would urge the Congress to resist any attempts to establish an additional procurement structure without a corresponding reduction of existing procurement activities.

Now I would like to turn to the second subject, that of an acquisition methodology which provides motivation for quality improvement.

Before I elaborate on some specific recommendations for rewarding contractor excellence, I would like to take a moment to discuss some of the peculiarities of the process of major system acquisition since they have a profound effect on both cost and quality.

The sophistication and complexity of modern major weapons systems dictate a lengthy cycle for acquisition. At the outset of the cycle, a system is conceived and designed to meet the specific known threats. But as the cycle continues through the development phase, those threats can change.

And the system, whether in the development or the production stages, must be upgraded to counter those evolving threats.

In addition, the acquisition cycle must accommodate product improvement prompted by several other factors, including changes in mission and doctrine, the desirability of lower life-cycle costs, and opportunities to incorporate new technology to increase system capability and reliability.

Today, the prevalent strategy to reduce costs and increase quality over the course of the acquisition cycle involves competition—

competition in the design and development phases and in the production stage. Indeed, this strategy has merit when sensibly applied.

Competition for major weapons systems already in production can drive cost reduction and quality enhancement, but only under a specific set of circumstances.

Procurement levels must be able to support more than one source.

Projected savings to the Government customer must exceed the capitalization costs inherent in dual sourcing.

And contractors must be able to recoup the capital investments they have made to achieve both production capabilities and a reduction in system costs.

Otherwise, competition simply does not make sense.

But I believe there are greater opportunities to reduce costs and improve quality after initial competition has been conducted and after contracts have been awarded.

Once a contractor has competed for and won a contract, and is providing a product or system that works the way it is supposed to, cost reduction and quality enhancement do not have to be competed into that program; they can be managed in, with the cooperation of the customer and the contractor.

And such cooperation carries handsome rewards for the Government.

There are examples of such results on many programs where we have used quality as a motivator to improve the end product and lower costs. Why not utilize what we have learned on these and add a positive dimension to our acquisition policy?

Jim Wade, the Assistant Secretary of Defense for Acquisition and Logistics, recently testified before this committee on the importance of quality in defense procurement. He said:

> Quality is at the top of my agenda for the future. The idea of "minimal quality" being sufficient in many cases must be replaced with a philosophy of continuous quality improvement * * * We intend to find new ways to consider quality history in the source-selection process and to reward high-quality performance.

Dr. Wade further said:

> In DOD acquisition, competition is too frequently based just on price, and an "award to the low bidder" mentality is too pervasive. As long as this persists, there is no reason for contractors to make quality a way of life.

Increased competition in procurement as in many cases proved to be in the best interest of the Nation. But we have to recognize that competition for cost is not the only answer and in some cases it may be the wrong answer.

On many existing major programs, the current contractor is already providing a good quality product at a reasonable cost.

Instead of competing these programs just for the sake of competition, why not put a higher priority on rewarding excellence, on finding incentives to motivate that contractor to make his quality even better, his price even lower?

For example, why not establish separately exercisable follow-on business options, specially allowing increased profit as a function of reduced cost goals?

For example, why not set site-specific improvement targets in our various overhead rates—engineering, manufacturing, G&A, and staff? And if we meet those improvement goals, allow us to share some of the improvement.

For example, if DOD works with us to develop real information on scrap, rework, and repair and then motivates us, not punishes us, with that data, both parties could win with improvement goals in these areas.

If reform of the procurement process penalizes those companies which violate acquisition rules and regulations, it should also reward those contractors who demonstrate excellence in performance.

If companies can receive new contracts and follow-on business in return for quality performance, they will provide quality. If they can share in the savings generated by their cost-cutting and quality-improvement efforts, they will cut costs and improve quality.

I believe this is fundamental to long-range reform.

It is time for Government customers and Government contractors to join the same team and dedicate that team's efforts toward the common goal of producing top-quality systems at acceptable costs.

We, therefore, urge this subcommittee to continue this serious and timely review of DOD's implementation of recent congressional enactments and to make oversight of such actions its first priority in the next year.

I would be happy at this time to answer any questions the subcommittee may have.

Thank you.

[The prepared statement of Mr. Rittenhouse follows:]

PREPARED STATEMENT OF JOHN RITTENHOUSE, EXECUTIVE VICE PRESIDENT, RCA AEROSPACE AND DEFENSE SYSTEMS, INC.

Mr. Chairman and Members of the Subcommittee, I am John Rittenhouse, Executive Vice President, RCA Aerospace and Defense, and I am pleased to appear here this morning on behalf of the Electronic Industries Association (EIA). The EIA is made up of some 500 electronics manufacturing firms, many of which provide products to the Department of Defense.

I thank the committee for the opportunity to be heard on a subject that is so critical to the future of our nation.

These is no question that there have been and still are problems in the way our nation has acquited the products and systems needed for its defense.

The deficiencies that do exist in our defense procurement process have evolved over years and decades, and all of us—industry, the Department of Defense, the military services, and the Congress—have contributed to difficulties we are experiencing today. For those problems to be eliminated—as they must be—all of us must work together, without fingerpointing or buck-passing. These hearings are a positive step in that direction.

To establish a framework for my remarks today, I'd like to outline three fundamental premises that are "givens" in discussions of defense system procurement.

In the context of these three fundamentals, I'll then provide you with some specific recommendations, from a contractor's point of view, on what can be done to improve the procurement process. These suggestions concern the reorganization of DOD's acquisition organization, and ways in which we might add a positive dimension to acquisition methodology based on rewards for quality improvement.

The first fundamental premise is that the primary goal of everyone involved in the defense acquisition process—private industry, the military, the civilian defense establishment and Congress alike—is to provide our servicemen and women in the field with high quality, reliable, affordable equipment, capable of meeting any threat to our national security.

I assure you that defense contractors do recognize the special trust and obligation that our work entails, an obligation that ultimately must transcend the profit motive.

The second fundamental premise is that, unlike most commercial industries, where the ability to cut costs and improve quality translates almost automatically into increased profit, defense is a cost-based business. Basically, that means that we have a different structure to earn profit--since profit is determined as a percentage of our cost.

As a result, in today's acquisition system, industry in many cases does not have enough real motivation to reduce its costs on a contract. Indeed, in some flexibly priced contracts, there are a good many disincentives to cut costs. And even in competitively won, firm-fixed-priced contracts, the motivation is to be only slightly better than the competition. There is no real long term incentive to lower costs, particularly since we may be locked into those established lower rates in subsequent bids on follow-on contracts and business. The solution does not lie in more legislation regarding competition, but rather in the adoption and implementation of positive incentives to reduce costs and stimulate efficiency, some of which I'll elaborate on later.

The third premise is that we have, over a period of years, decided that we can't field a numerically superior force, so we must field a technologically superior, reliable force structure.

In our haste to improve the acquisition process, we have focused on competition as a means of ensuring the affordability of defense procurements. And indeed competition in many instances has been a powerful tool for lowering costs.

But competition alone will not insure meeting our objectives. Detailed and exquisite certification of rate structures may satisfy the need for accountability, but it does little to improve the quality of product.

Ultimately, we must not only achieve cost reduction, but we must also achieve reliable equipment with technological superiority. Such a task will require a procurement organization that can deal with all the issues, and an incentive approach for industry which makes improved quality a new industry objective.

And so, I'd like to turn to the area of organization first.

Today's acquisition environment is indeed complex. In contrast with the scenario a few years ago—when a strong government program manager was the central figure of product and administration authority—we now find diffused responsibility amongst a variety of military and civilian implementation and monitoring agencies.

Today, a great many of the program decisions are made within the OSD and Congress, and a new power structure has emerged within the civilian secretariat.

Within OSD, acquisition authority is diffused, through assistant secretaries for Acquisition and Logistics, Research and Engineering, C3I and others. Somewhat similar authority centers exist within civilian organizations of the military services. And Congressional staffs have grown in size, expertise and influence.

In just the past two years, Congress has imposed major reforms on the procurement process, including: The Competition in Contracting Act (CICA); Warranties, and other procurement policy matters addressed in the Small Business and Federal Procurement Competition Enhancement Act of 1984.

Because of the breadth of the reforms and the speed at which they were enacted, DOD has naturally found it extremely difficult to implement the intent of these laws, even in instances where Congress simply codified existing concepts.

Let's examine one such revision, perhaps the simplest of them all. On February 28, 1984, as one of its spare parts initiatives, DOD directed the services to provide under contracts for commercial parts that the price being charged to the government, all other things being equal, is no more than the lowest price charged to the most favored commercial customer. This was subsequently codified in brief and simple terms in P.L. 98-525 and P.L. 98-577 in October 1984. Congress adopted the simple, clean terms of the DOD direction.

DOD's implementation of this statute has yet to be accomplished. It took nine months to effect what should have been a simple revision, and this was without public comment on the basis of "public exigency." The result was language so far afield from Congress' intent that OMB, in an unprecedented action, disapproved the regulation on the basis of its content rather than its form.

As a result of the burden placed on DOD, implementation of the law is lagging, and there is great disparity in interpretation between DOD and civilian agencies and among elements of DOD itself. We believe that it is incumbent on Congress to insure uniform, concise, and timely dissemination and implementation of legislative reforms. As things currently stand, multi-source management and hastily-prepared directives result in a great deal of confusion for industry.

In another example, Secretary Weinberger authored a new requirement for the certification of all overhead cost submissions, under penalty of perjury.

In the six months since that mandate was issued, we have seen the issuance of: Two clarifications by DOD's legal Counsel; two clarifications by the Deputy Under Secretary of Defense for Acquisition Management; two clarifications by the Chairman of the DAR Council; a DAR Council issuance as a temporary regulation; a revised temporary regulation; and no final regulation.

Each service and the Defense Contract Audit Agency (DCAA) was left to accomplish implementation in a wide variety of contradictory ways. The resulting confusion in the field has created situations in which negotiations have stopped completely, and companies have seen their progress payments and final payments needlessly stopped. Some proposals are being audited, others not, and many companies are unable to settle final overhead rates dating back to seven years.

The government manager once had primary responsibility for, and control of, acquisition of major weapon systems. However, the role of the program manager has been considerably diminished in recent years.

Source-selection decisions once made by one responsible individual now are reviewed by Source Selection Evaluation Boards and made by Source Selection Authorities, after which the selections are subject to higher-level approvals.

A source decision may have to be approved by a Competition Advocate, the head of the procuring activity, the senior procurement official of the agency, even the Secretary of Defense, resulting in considerable delay in the procurement process.

Source decisions may be questioned by Competition Advocates, breakout specialists or Small Business Advocates, delaying the process even further.

Also adding to the confusion over responsibility is the split of authority between the contracting officer and the auditor.

Price decisions cannot be made without audit review, and formal justification must be prepared if the contracting officer disagrees with the auditor.

Increasingly, authority in such areas as determination of contract rates has been transferred from the contracting officer to the auditor.

That development is just one example, by the way, of another major problem in our defense procurement system—the growth in recent years, in terms of both size and power, of a diverse acquisition monitoring organization that is the second major group impacting on today's acquisition process.

DCAA, DCAS, GAO, and IGs, OSHA, EPA and the Department of Labor are only a few of the government entities now involved in acquisition monitoring, in the areas including Allowable Costs, Overhead Rates, Pricing, Quality, Environmental Concerns, Workers Health and Safety, Minority and Small Business Subcontracting, and the list goes on and on.

Government audit functions alone are engaged in, at any given time, approximately 40 separate audits within RCA Aerospace and Defense. RCA, in turn, must allocate personnel to interface with each of these government auditing units.

We certainly recognize the need for oversight, by the demands of dealing with the flood of audits, investigations and review in our industry are consuming an ever-larger portion of our human and financial resources, and the cost of all this must be recovered in the prices contractors charge the government.

As I indicated earlier, over the past ten years a substantial measure of authority for government acquisition has shifted to the Congress—the third major entity affecting the procurement process.

In 1975, four congressional committees were writing legislation involving defense issues, including procurement. Today more than 60 congressional committees and subcommittees find defense-related issues on their agendas.

Committee staffs have experienced a corresponding increase in size and expertise, and now are equipped to address in greater detail procurement aspects such as cost, schedule, programmatics and technological issues.

While increasing congressional involvement in the procurement process has been beneficial in many ways, some legislative initiatives have had a negative impact on the process, due in part to varying interpretations by the DOD, the military services, and industry.

For example, there have been legislative efforts by Congress to encourage wide use of work measurement standards throughout the defense industry. These efforts would only affect a small percentage of total product costs, and could easily be outweighed by additional administrative costs.

Such standards, specifically MIL-STD-1567A, are an example of how well-intentioned efforts at procurement reform have proved to be counter-productive.

There have been various efforts over the past decade or so to implement extremely detailed work-measurement standards in the defense industry, but in my opinion, such standards simply aren't compatible with enlightened quality conscious management.

Unlike progressive concepts such as work centers, participative management, automation, cross training and work sharing, the focus of 1567A is on the individual worker, rather than the work group.

Moreover, measurable "tough" labor, the target of these standards, in most cases is, . . . and should be . . . a minor cost factor in modern defense manufacturing, representing only about six percent or less of total product cost.

And practices such as Just-in-time, Manufacturing Resources Planning programs, flexible manufacturing systems, computer-integrated manfacturing and robotics are making touch labor cost even less significant.

Work-measurement standards are of particularly dubious value in areas of the defense industry such as satellites and large radar systems, where low-volume, long-cycle programs predominate and where products continually push the technological state of the art.

My message is simply this: MIL STD 1567A will in many instances add to the cost of a product, not reduce it, and will have little, if any, positive effect on quality.

In an increasing number of situations, it costs more to measure performance, in the exact terms demanded by 1567A, than the touch-labor cost of manufacturing the product itself!

Although such measures are born from frustration with out industry, it seems more appropriate to charge an authoritative acquisition entity with the responsibility to implement corrective action, rather than invoke specific detail via the legislative route.

I can assure you that industry wants to assist Congress in its efforts to reform the procurement process. But a fair, cost-efficient procurement system can exist only in a stable environment, and many of the recent efforts at reform have in fact contributed to increase instability in the system.

I've outlined just a few examples of such destabilizing factors in the areas of acquisition organization, acquisition monitoring, and congressional oversight.

I would urge Congress to refrain from taking any additional initiatives until these changes have been assimilated by the system, and I recommend that the Packard Commission, as it has come to be called, be given time to make a balanced, thoughtful and complete examination of the many complicated issues involved before any plan for procurement reform can be enacted.

I will follow my own advice then, and await the Packard Commission's assessment of just how the acquisition process should be specifically structured. But I do urge you to consider three elements that true reform of the process demands:

1. A single well-defined procurement chain within the Department of Defense.
2. A single well-defined monitoring and auditing authority.
3. A single well-defined structure for Congressional inquiry and oversight.

In other words, please decide who's in charge.

Also, I would urge the Congress to resist any attempts to establish an additional procurement structure without a corresponding reduction of existing procurement activities.

Now I'd like to turn to the second subject, that of an acquisition methodology which provides motivation for quality improvement.

Before I elaborate on some specific recommendations for rewarding contractor excellence, I'd like to take a moment to discuss some of the peculiarities of the process of major system acquisition since they have a profound effect on both cost and quality.

The sophistication and complexity of modern major weapons systems dictate a lengthy cycle for acquisition. At the outset of the cycle, a system is conceived and designed to meet the specific known threats. But as the cycle continues through the development phase, those threats can change. And the system, whether in the development or the production stages, must be upgraded to counter those evolving threats.

In addition, the acquisition cycle must accommodate product improvement prompted by several other factors, including changes in mission and doctrine, the desirability of lower life-cycle costs, and opportunities to incorporate new technology to increase system capability and reliability.

Today, the prevalent strategy to reduce costs and increase quality over the course of the acquisition cycle involves competition—competition in the design and development phases and in the production stage. Indeed, this strategy has merit when sensibly applied.

Competition for major weapons systems already in production can drive cost reduction and quality enhancement, but only under a specific set of circumstances.

Procurement levels must be able to support more than one source, projected savings to the government customer must exceed the capitalization costs inherent in dual sourcing, and contractors must be able to recoup the capital investments they have made to achieve both production capabilities and a reduction in system costs.

Otherwise, competition simply doesn't make sense.

But I believe there are greater opportunities to reduce costs and improve quality after initial competition has been conducted and after contracts have been awarded. Once a contractor has competed for and won a contract, and is providing a product or system that works the way it is supposed to, cost reduction and quality enhancement don't have to be competed into that program; they can be managed in, with the cooperation of the customer and the contractor.

And such cooperation carries handsome rewards for the government.

There are examples of such results on many programs where we've used quality as a motivator to improve the end product and lower cost. Why not utilize what we've learned on these and add a positive dimension to our acquisition policy?

Jim Wade, the Assistant Secretary of Defense Acquisition and Logistics, recently testified before this committee on the importance of quality in defense procurement. "Quality is at the top of my agenda for the future," he said. "The idea of 'minimal quality' being sufficient in many cases must be replaced with a philosophy of continuous quality improvement . . . We intend to find new ways to consider quality history in the source-selection process and to reward high-quality performance."

Dr. Wade further said, "In DOD acquisition, competition is too frequently based just on price, and an 'award to the low-bidder' mentality is too pervasive. As long as this persists, there is no reason for contractors to make quality a way of life."

Increased competition in procurement has in many cases proved to be in the best interest of the nation. But we have to recognize the competition for cost is not the only answer and in some cases it may be the wrong answer.

On many existing major programs, the current contractor is already providing a good quality product at a reasonable cost.

Instead of competing these programs just for the sake of competition, why not put a higher priority on rewarding excellence, on finding incentives to motivate that contractor to make his quality even better, his price even lower?

For example: Why not establish separately exercisable follow-on business options, specifically allowing increased profit as a function of reduced cost goals?

For example: Why not set site-specific improvement targets in our various overhead rates—engineering, manufacturing, G&A, and staff? And if we meet those improvement goals, allow us to share some of the improvement.

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If reform of the procurement process penalizes those companies which violate acquisition rules and regulations, it should also reward those contractors who demonstrate excellence in performance.

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I believe this is fundamental to long-range reform.

It is time for government customers and government contractors to join the same team and dedicate that team's efforts toward the common goal of producing top-quality systems at acceptable costs.

We therefore urge this subcommittee to continue this serious and timely review of DOD's implementation of recent Congressional enactments and to make the oversight of such actions its first priority in the next year.

Senator **Quayle**. Thank you very much for a fine presentation.

The next witness is Mr. Charles Stewart, president of the Machinery & Allied Products Institute.

Mr. Stewart, welcome.

STATEMENT OF CHARLES W. STEWART, PRESIDENT, MACHINERY AND ALLIED PRODUCTS INSTITUTE, ACCOMPANIED BY WILLIAM HEALEY, VICE PRESIDENT OF LAW, MACHINERY AND ALLIED PRODUCTS INSTITUTE

Mr. STEWART. It is a pleasure for MAPI to appear before this subcommittee. I am accompanied by William Healey, MAPI vice president of law.

As you will observe, the specific comments in our statement which I will summarize are keyed for the most part to the testimony of Assistant Secretary Wade of the Department of Defense before this subcommittee on October 17. In this summary I will merely try to hit the high spots.

First, I think it is fair to say that it is a little early to evaluate fully the impact of the procurement legislation recently enacted. Some of the legislation contains deferred effective dates, and institutionalizing of procurement law changes sometimes takes 3 to 5 years.

Hence, there will be a further need for the kind of retrospective look you are trying to take in this hearing.

You will note that there will be in my summary and in the full text some repetition of points made by Mr. Rittenhouse. I trust this has the virtue of emphasis.

Now, to some points that I would like to emphasize.

First, it is our view that it is important for the Congress to resist further procurement legislation and further expansion of administrative controls by procurement authorities, notably the Department of Defense, at least for a period of time.

Within the last 2 years the Congress has been generating new legislation at an incredible rate in this area. As long as these new laws remain on the statute books, they must be implemented by regulations and directives and lived with by both procurement authorities and defense contractors.

This is an enormous task and, as I mentioned earlier, it takes 3 to 5 years to institutionalize major changes in the law. In this connection, I refer to the pending appropriation legislation which has been passed by the House, and which would tighten by amendments the legislation that was adopted for procurement purposes in the authorization bill.

Mr. Chairman, I notice that you had certain frustration about the delay in getting House action on the Authorization Act. I trust that when the Senate addresses the appropriations changes in respect to procurement that they will be rejected. We do not need more law.

Second, we feel it is incumbent on the Congress and to some extent on the Department of Defense to build a comprehensive record of defense industry technological accomplishments which are extraordinary.

At page 2 of our statement we identify certain examples at random. I have additional information with me if the subcommittee is interested.

I note in the Congressional Record for the House proceedings on October 30 that Congressman Miller of Ohio made the same point which I offer at this time.

Third, under this administration a number of acquisition priorities have been developed and placed in effect. There are certain inherent conflicts between these priorities. In our opinion, it is the obligation of the Congress and the procurement authorities to identify these conflicts and reconcile the priorities.

Otherwise, the will of the Congress and the intent of the procurement authorities in an overall sense will be thwarted and we will confront at least to some extent the danger of chaos in the system. I refer here to such priorities as competition, quality, incentives for utilization of advanced technology and production, protection of proprietary rights, maintenance of an adequate industrial base, et cetera.

Fourth, oversight by the Congress in participation in the legislative process involving procurement legislation is grossly overdone, in our judgment, in terms of the number of committees, subcommittees, hearings, required reports to the Pentagon and, if I may use the word, at times, inquisitions.

As a long-time observer of the congressional and executive branch scene, I do not know how the legislative process in respect to procurement policy can operate effectively under these conditions. The implementation burden placed on the procurement authorities is unbelievable and unsustainable, in my opinion.

The Congress should undertake, I respectfully request, a narrowing of the role of oversight and committee activity in legislation insofar as procurement policy is concerned. This, of course I recognize, will require a delicate balancing of congressional deference and organizational discipline.

Fifth, the Congress is appropriately concerned with cost in the procurement area, but it stops short of examining a key element of cost. I refer to the proliferating cost of control and regulation. This is a real challenge to the Congress and to the procurement authorities to quantify.

In my opinion, a careful examination of the cost of control and regulation will justify limiting further expansion of controls and regulation and may very well trigger some reduction in the control apparatus.

In this measurement process special attention should be given to the exploding cost of the audit function, and in examining cost, direct costs should, of course, be determined, but indirect cost impacting on the contracting process and the weapon production effort should also be examined.

I refer here to bogging down of defense production, diversion of contracting personnel, both Government and industry, from such objectives as quality, et cetera.

Dr. Edward Luttwak of Georgetown University, and Dr. Gansler of the Analytic Sciences Corp. were speakers at a recent meeting of the National Contract Management Association. It was said by these two gentlemen that perfection in the procurement process, including total competition, is not cost effective.

Dr. Luttwak thinks it was a waste of money for the Air Force System Command to add 3,000 people to deal with the acquisition of spare parts. These 3,000 people cost a lot more than the overpriced portion of spare parts.

Both of these gentlemen also agree that there will always be mistakes because it is not cost effective to be perfect.

Harvey Gordon, director of business government policy at Martin Marietta, stated it best when he said there must be a meaningful distinction between doing a job well and perfectly.

Sixth, the Congress and the procurement authorities should undertake a joint investigation of the relationship between project managers, contracting officers and auditors. It has become deliberate policy to give overriding authority to the auditing function with the result of the project manager and contracting officer in particular are relegated to lesser roles and deprived of certain incentives which are necessary to achieve the best results.

With respect to the degradation of the authority of the contracting officer, William W. Thurman, Deputy Director of the National Security Division of the General Accounting Office, said at the recent conference I referred to that DOD has completed a 1½-year study to be released shortly, of the career path of Government program managers and contracting officers and has found evidence of micromanagement.

Decisions are being made at the secretariat level in the military services instead of by the program managers and contracting officers.

Also, whatever decisions the program manager and contracting officer are allowed to make are scrutinized by a plethora of checkers. He distinguished between doers and checkers such as competition advocates and streamline advocates required by recent reform legislation.

Professor Cbinic, also a speaker, went so far as to say that the contracting officer in today's contracting system is a legal fiction.

Darleen Druyun, the Government procurement expert on technical data, was also in this conference and she made some very interesting comments about the quality of contract work performed by Government procurement personnel, saying that it has declined. She attributes this decline to several factors, including:

A 30-percent change in the procurement regulations since the FAR was implemented on April 1, 1984, which was primarily due to the three 1984 statute.

The increased complexity of contracting due to the three statutes.

The degraded authority of the contracting officer.

DCAA, incidentally, has been granted authority to negotiate all final indirect cost rates at contractor plants, preempting the contracting officer.

Constant negative publicity.

A significant workload increase without proportionate increase in contracting personnel. There has been a 30-percent increase in contract actions, she says, from 1983 to 1985.

The goldfish bowl environment in which contracting people work. She mentioned, for example, that one Air Force plant representative office, which employs about 100 persons, had an average of 400 visitors a month.

Seventh, Congress should also examine what appears to be the development of certain autonomous procurement postures and actions by individual services.

The corollary to that proposition is that there is some evidence that the Department of Defense at OSD level is not monitoring this problem adequately and not exercising sufficient centralized control over the services. We need a single set of procurement policies, not a multiple set.

Next, I call attention to our comment on proprietary data and the importance of maintaining a sound and strong industrial base at the prime and subcontractor and subsubcontractor levels. Do not tolerate blunting of contracting incentives by unwarranted taking of proprietary rights.

Next, a comment on implementation of the three procurement statutes oversight, at this time, as I have already mentioned, must be preliminary for the reasons given.

Now I will close. I am submitting our full statement for the record and in an effort to summarize it within your time schedule, I want to emphasize that MAPI and I personally are very conscious of the responsibilities of the contracting community at large and individual contractors at all levels to take an ethical approach to this contracting role, to apply to the maximum extent possible internal controls, to abide by the law and regulations and, above all, to make maximum contribution to the ultimate objective of the acquisitions process which is so often lost in that process.

That ultimate objective is to furnish the highest quality products at a reasonable price and with timely delivery.

It is only against this background that I have presumed, with due respect to the subcommittee, to make suggestions regarding some studies that might be undertaken by Government and to offer criticisms which we feel are constructive and in the public interest.

To add a word, we recognize the duty of the private sector active in the defense acquisition process to respond affirmatively to well-founded criticisms of performance even though they may have to tolerate at times some criticisms that are not well founded.

Thank you.

[The prepared statement of Mr. Stewart follows:]

MACHINERY AND ALLIED PRODUCTS INSTITUTE

Statement of the
Machinery and Allied Products Institute
to the
Defense Acquisition Policy Subcommittee
Senate Armed Services Committee
on
Recent Procurement Legislation and Its Implementation

November 7, 1985

Introduction

We appreciate the opportunity to discuss, at least in a preliminary manner, the legislation enacted last year on procurement and the status of its implementation. More specifically, the Subcommittee seeks comments on implementation of the Competition in Contracting Act, the Defense Procurement Reform Act of 1984, and the Small Business and Federal Procurement Competition Enhancement Act of 1984. I indicate that we will comment in a preliminary manner because the implementation process is by no means complete and, because of deferred effective dates contained in the legislation, the impact even when the statutes are implemented has been postponed to some degree. In addition, for other reasons, it is a little early to obtain constructive reactions from industry on the effects of the legislation.

First, a word about MAPI. As the Subcommittee may know, MAPI represents the capital goods and allied product industries of the United States. In addition to traditional capital goods product lines, MAPI's constituency includes leading companies in the electronics, precision instruments, telecommunications, computer, office systems, aerospace, and similar high-technology industries. Although many of the companies in these industries are predominantly oriented towards the commercial market, a significant number have substantial defense sales at the prime and/or subcontract level and, accordingly, have a particular interest in government contracts. This accounts for their concern with any legislation which might adversely affect contractors in their relationship with the government and, indeed, impact the public interest adversely.

I should add that we must be especially sensitive to the problems at the subcontracting level, which too often are overlooked or given only limited consideration.

Extraordinary Contribution to National Security by Defense Industry: Need for Public Recognition by the Congress and Procurement Authorities

The Congress and procurement authorities have become so preoccupied with enacting in statutory form and promulgating administratively controls and regulations on defense industry that the critical role of contractors in innovation and production of sophisticated, complex, and absolutely critical defense products is being subordinated.

Let me cite at random a few examples. The performance of the shuttle and its role in commercial and defense activities have almost been overlooked in the rhetoric. This is a remarkable achievement and it is being taken for granted. The B-1B record in terms of technological accomplishment and delivery on schedule is outstanding. The recent intercept by Navy fighter aircraft in the Mediterranean was accomplished with the application of extraordinary technology and military performance and yet the Congress, and particularly the media, apparently would rather talk about so-called horror stories. Much of the same can be said for contributions in the missiles area, e.g., the Patriot and the Titan. The M2/3 Bradley Fighting Vehicle is another example of leading and vital technology. And we should not overlook the classified and critical contributions of defense industry to the Defense Advanced Research Projects Agency (DARPA) and to the Strategic Defense Initiative (SDI). Further, don't overlook the contribution of thousands of subcontractors to such programs. In connection with the availability of such information, attention is called to the publication of the Association of the United States Army (1985 Edition) entitled "Issues Impacting on the Land Forces of the United States." MAPI hopes to develop this aspect more fully in oral testimony, but it is emphasized here preliminarily.

Let me carry the point one step further. Why shouldn't this Subcommittee call a hearing on the technological achievements jointly accomplished by defense industry and procurement authorities? The American people are entitled to this information and to a balancing of the record. If you pursue this suggestion, I recommend that you issue a report rather than depending on the media to report results.

Specific Comments Keyed to Testimony of DOD Assistant Secretary Wade

Our statement uses as a launching base the testimony of The Honorable James P. Wade, Jr., Assistant Secretary of Defense (Acquisition and Logistics) before this Subcommittee on October 17. Proceeding in this manner, we will quote from Assistant Secretary Wade and then offer pertinent MAPI comments at each juncture. The material taken from Assistant Secretary Wade's presentation is indented in quotations; then our observations follow each quotation.

Need for caution in adopting new statutory rules.--

> ". . . While we would have preferred to perfect the procurement system, including manpower, requirements, quality and process through regulatory reform, we are pursuing the course of action that Congress has laid out. . . ."
>
> "However, we must be cautious about laying down statutory rules that may inhibit our flexibility to take advantage of research and technology advances. . . ."

With one exception, we agree with both observations of Assistant Secretary Wade. In our judgment, Congress has over-legislated in the procurement area within the last two years and is practicing what has been commonly called "micromanagement" of the acquisition process. This will eventually bog down the essential role of acquisition which is to procure a high-quality product in timely fashion and at a reasonable cost. The risk from excessive control of the system is that the United States will be buying more controls and less product.

The regulatory process and its impact are very costly and the Congress would be well advised to attempt to measure the cost of regulation in this area. I think you would be surprised by what you find.

The exception to which I refer is that excessive control and over-regulation can be invoked administratively by the Department of Defense in the same way that Congress might over-legislate. And it is our feeling that the Department of Defense is moving in the direction of excessive control on its own initiative. A current example of administrative overreaching is the proposed regulation on technical data to which I will refer in more detail later; another illustration is the DOD Certificate on Overhead Cost which was a classic example of bad draftsmanship and regulatory abuse.

Let me dramatize the proposition of overregulation and micromanagement. The trend is so strong in statutory enactment and in the philosophy and content of administrative regulation by procurement authorities that we may be on the road to the equivalent of nationalization of defense industry. It would be premature and extreme to conclude that we have reached that result but the direction is clear. And believe me government is in the very risky business of pushing in that direction and yet having no responsibility for the end-product in terms of procurement results. Let us all ponder this suggestion of direction.

In this connection, I draw the Subcommittee's attention to the interchange between Senator Quayle and Assistant Secretary Wade during the question period following his testimony on October 17. Assistant Secretary Wade backed off from the view expressed in his principal testimony that Congress was over-legislating in the procurement area and that so much legislation might create a "rupture" in the acquisition process. I think this deviation from Mr. Wade's principal testimony was unfortunate, whether or not inadvertent. Not only has there been too much legislation, its detailed nature compounds the problem.

The Competition in Contracting Act and the role of competition generally.—

> "The Competition in Contracting Act of 1984 (CICA) has received the most attention in and outside the government since its provisions are applicable to all government agencies. . . . The real impact of this Act will occur in FY 1986 as a large number of solicitations for major programs were issued before April 1, 1985 and thus the Act did not apply. . . . Our objective is to pay a fair and reasonable price for quality supplies and services. Competition is one method for achieving that objective where it is practicable and possible."

As Assistant Secretary Wade points out, measurement of the real impact of this Act must be deferred because of the effective date. Some preliminary observations, however, seem to be in order. The recognition in the new law that negotiation can be competitive is a step forward. Sealed bidding has no monopoly on competition and is inappropriate in many procurement situations.

Having said that, it is important for the Congress and procurement authorities to recognize that fair and reasonable contract pricing is the basic objective, and competition is merely one method of achieving that objective. Competition should not be forced into the process where, as Assistant Secretary Wade indicates, it is not practicable or possible. Achievement of competition in certain situations can be very costly and not productive. The process of "creating" a competitor from scratch may not work and, even if it does, may be very expensive. In a way, striving for competition in government procurement runs the risk of attempting to transfer a commercial concept widely practiced with success in the commercial world but not always appropriate to government procurement, particularly when you are dealing with advanced and very complex systems.

Attempts to achieve greater competition also may cause conflicts with other procurement criteria and objectives. To illustrate, to achieve greater competition the procurement system should not sacrifice quality of product. Nor should it jeopardize unfairly proprietary rights of a contractor who has brought initiative and innovation to the procurement process.

Further, competition requirements frequently are driven by socioeconomic objectives which, although meritorious in general, often are not conducive to sound procurement policy.

Contractor rights in data.—

> ". . . [C]overage concerning technical data requires careful balancing of the need to acquire the rights in technical data for the purpose of enhancing competition while not stifling the initiative of American industry to develop leading edge technologies without government funding."

The Assistant Secretary is right on target with this statement. But he goes on to acknowledge that critics of DOD's proposed rule on acquisition of technical data:

> ". . . believe that we went beyond the statutory language of what is realistically do-able. Upon reflection, we agree with the sense of the reaction and will revise our implementation to be in accord with the statutory provisions."

This is an example of the draftsmen at the DOD overreaching, as previously indicated. In this connection, the handling of this matter was at a high level in the Department of Defense. MAPI comments to the Department of Defense on the proposed rule are attached as Appendix A to this statement. Moreover, MAPI's representations to the Pentagon on this issue took place over an extended period prior to our comments on the proposed rule.

The validation-of-restrictions regulations raise problems because they would permit contractor restrictive markings to be canceled prior to the final disposition of litigation, if the government finds that "urgent and compelling" circumstances will not permit awaiting the end of the litigation. DOD and the services seem to determine with relative ease that such circumstances exist.

Beyond the question of implementation of the statutory provisions, it is our view that the law itself may be defective in certain respects, and we encourage the Subcommittee to reexamine it. Most importantly, on this point there is the issue of the "cap"--the term of years after which the government would have the right to use contractor data without restrictions. It would seem that if there is to be such a cap, the statute should include a detailed statement of criteria governing its use.

Absorption of new statutory provisions could bog down procurement.--

> ". . . It is a most difficult task for our procurement personnel to absorb these wide-scoped changes and yet continue to purchase supplies and services to clothe, feed, house, train, and provide weapons to our field forces. I am somewhat amazed that there has not been a major rupture in the acquisition process. . . ."
>
> "I would strongly recommend to the committee that it resist further procurement reform legislation until we have had a year or two to assess the impact, improvements, and deficiencies of the legislation enacted. The pending DOD authorization bill for FY 1986 contains a number of additional procurement reforms. I think this is unfortunate. . . ."

The Assistant Secretary makes a valid point. Not only does the authorization bill for FY 1986 contain a number of additional procurement reforms, but the Reagan Administration has now submitted to the Congress another package of legislative recommendations in the procurement area which it calls the "Anti-Fraud Enforcement Initiative" legislative package. There is just too much legislation in the procurement area and, secondly, the Congress does not seem to appreciate fully the implementation burden which this stream of legislative enactments imposes.

"Horror stories" not indicative of procurement as a whole.--

> "I believe the vast majority of the current legislation is based on the premise that the DOD needs assistance in reforming the way we purchase systems, equipment, and materiel. The impetus for many of these reforms has been the seemingly daily 'horror stories' on hammers, coffee pots, or other spare parts. Whether they are individually justified or not, these stories fortunately are not indicative of our current acquisition system as a whole. A sense of proportion, as I alluded to earlier, is lacking."

We agree with the spirit of these comments, although in no way does MAPI wish to challenge the oversight authority and responsibility of the Congress and its cognizant committees. A sense of "proportion," to which Assistant Secretary Wade refers, certainly needs to be applied.

Quality as a goal.--

> "Quality is on the top of my agenda for the future. . . . This concept of minimal quality must be replaced with a philosophy of continuous quality improvement. In DOD acquisition, competition is too frequently based just on price, and an 'award to the low bidder' mentality is too pervasive. As long as this persists, there is no reason for contractors to make quality improvement a way of life. . . . We plan to move away from defining equipment requirements in minimally acceptable terms to a system whereby the best quality equipment at an acceptable price is our recognized objective."

Note the reference to competition too frequently being based just on price.

I am sure that defense industry will cooperate in every way possible with the goals laid down by the Assistant Secretary in reference to quality and achievement of high-quality performance. But both the Congress and procurement authorities must recognize that certain objectives espoused by the Congress and to some extent the procurement authorities, such as an apparent attempt to achieve competition as an absolute goal, are not necessarily consistent with the realization of high-quality performance. To illustrate further, the explosive growth of the audit process interferes with concentration of the contractors on innovation, production, and on-time delivery of quality products. Moreover, overregulation of the defense industry in general is not conducive to maximizing high-quality performance.

With respect to quality, this is a goal that is exceedingly important in commercial business as well as in defense production. I refer the Subcommittee to the new book, The Wall Street Journal on Management[1], in particular to the article entitled "Improving Quality: Lessons From Hewlett-Packard" by John A. Young, President and Chief Executive Officer of that company.

Role of DOD in promoting manufacturing and productivity improvement.--

> "Perhaps most significantly, with an annual procurement budget in excess of $100 billion, the DOD is playing a leading national role in promoting manufacturing and productivity improvement important to the economic revitalization of our nation."

Once again, I feel that defense industry will cooperate in every way possible in the achievement of this objective. On the other hand, it is fair to ask that both the Congress and the procurement authorities examine each procurement technique, policy, and control to determine if it hinders or contributes to the role

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1/ The Wall Street Journal on Management: The Best of the Manager's Journal, Edited by David Asman and Adam Meyerson, Dow Jones and Company, Inc., 1985, pp. 51-54.

described by the Assistant Secretary. For example, does the cutback in progress payments hinder the achievement of this objective? Do cost disallowances, such as interest and certain of those disallowances recently legislated, burden the contractor's ability to modernize? Assistant Secretary Wade, for example, states that he is looking for ways to revamp and restructure existing programs and policies to further promote this objective of achieving manufacturing and productivity improvement. We commend him for his willingness to engage in this revamping and restructuring process, and he should be zealous in identifying conflicts between policies.

The acquisition workforce.—

> ". . . [T]here are a number of actions we can take to enhance our acquisition workforce. We must also instill all individuals (extending to defense contractor personnel) better discipline and a sense that it is 'our' money being spent and not someone elses. We also need superior, better qualified people. . . ."

I am sure that in a general sense industry agrees with this statement. It is appropriate on this point, however, to indicate that Congress seems to mandate the granting of superior authority to auditing personnel over the contracting officer. This trend is disturbing to industry and, we believe, to government contracting personnel. We are convinced it will be counterproductive in the long run and it does not contribute to the broad objective of acquiring superior, better qualified people in the contracting officer corps. Moreover, excessive preoccupation with audit and granting of superior authority to the auditor over the contracting officer may very well distract the defense contractor from some of the other objectives of the Congress and the procurement authorities, including the overriding goal of obtaining the highest quality product, on schedule, at a reasonable price.

At some point the Subcommittee should examine the responsibilities and interaction between project managers, contracting officers, and various levels of the auditing corps. I suspect that you would find, for example, that the growing domination of the auditors is forcing the contracting officer into a posture of no-risk—not a favorable development for the procurement system.

DOD/industry relationship.—

> "Much has been said about the proper relationship of the DOD and industry. It is usually characterized in terms of being too adversarial or too incestuous depending on one's viewpoint. We have to be very careful that neither extreme is a reality."
>
> "One concern I currently have is that we may be placing too much emphasis on the threat of criminal penalties. We don't want to end up in this situation where crooks are the only people willing to do business with the DOD—since they may be the only type oblivious to the risks."

This is a valid point articulated in an effective way.

Some Other Observations

Needed amendment of Overhead Cost Certificate.--The Overhead Cost Certificate, which was very badly drafted by DOD, has been the subject of interpretation and clarification in certain Department of Defense documents. The Certificate itself, however, has never been modified directly. There is no excuse for this failure on the part of the Department of Defense, and we urge that this Subcommittee or its staff encourage appropriate corrective action by DOD to spell out what is the current actual policy concerning this certification requirement.

Warranties.--The new statutory provisions on warranties appear to have eliminated most of the problems implicit in the enactment of the Andrews amendment. It should be mentioned, however, that there appears to be some feeling that there has been insufficient implementation of the new provisions by the Office of the Secretary of Defense, thus permitting the individual services to go their own way on this matter.

As a matter of fact, in general, certain individual service procurement policies are too independent of overall DOD policy guidance. This trend seems to be expanding and accelerating. If we are correct, a major DOD organizational issue is raised and it should be addressed by the Congress and the President's Blue Ribbon Commission on Defense Management.

Defense industrial base.--Let me make a few comments on this subject. I think only lip-service is being paid to this vital issue.

The Congress should be aware that subcontractors are a critical part of this base. Many of them not only manufacture essential products but in a large number of cases they have commercial alternatives. Overregulate them and at least some will leave the defense procurement chain. In this connection, if procurement people overdo the price factor in overseeing prime contractor placement of subcontracts, including pushing for foreign sources, the U.S. subs will, of course, be turned off.

Publication of proposed regulations.--Although technically speaking the Office of Federal Procurement Policy statute is not within the purview of this particular hearing, we offer a pertinent comment for the information of the Subcommittee. The provisions of the OFPP Act require that no procurement policy directive shall take effect until 30 days after it is published for comment in the Federal Register. However, there is provision for waiving the requirement if urgent and compelling circumstances make compliance impractical.

DOD used the exception to put the new overhead cost certification requirement into effect last March without prior public comment. Subsequently, DOD, together with NASA and GSA, used the exception with respect to the commercial pricing certification requirement and the other provisions included in FAC 84-10 and FAC 84-11. At this point, the exception has been used so often that it is close to becoming the general rule. At the minimum, what needs to be done is to make clear to DOD that the exception proviso should be used only in a limited manner and that, when used, the "urgent and compelling circumstances" should be clearly identified.

Commercial pricing for supplies.--There is a requirement that in noncompetitive contracts the offeror must certify in his offer that the price stipulated is not more than its lowest commercial price for the item. This provision was implemented on an interim basis in FAC 84-10. We have criticized this regulation and our recommendations are spelled out in Appendix B to this statement.

Conclusion

In conclusion, we emphasize, respectfully, that in our judgment the oversight objectives of this Subcommittee are difficult to achieve fully at this juncture with respect to legislation so recently enacted, not yet fully implemented, and not yet tested in the field in a practical way. We wish, however, to commend the Subcommittee for its continuing role in reviewing and testing legislation enacted in the defense procurement area. Moreover, we believe that it is the Armed Services Committee--and this Subcommittee particularly--which should exercise the primary oversight role in the Senate with respect to DOD's procurement policies and activities.

We emphasize our view, which the procurement authorities seem to share, that in the government interest, and in the interest of the defense contracting industry as it attempts to assist in the achievement of national security objectives of the United States, we have already had more legislation than we need.

Beyond the specifics of individual statutory enactments, their implementation, and regulatory initiatives undertaken by procurement authorities without reference to statutory mandates, we see an already existing and growing problem of substantial magnitude in the congressional oversight process as it relates to the defense program of the U.S., including procurement. There are so many committees, subcommittees, and congressional staff playing a role in the oversight process in the Congress that we have difficulty understanding how the Congress can effectively legislate in this area and how procurement officials can find the time to manage their responsibilities. The total number of procurement-oriented hearings and special congressional requests to procurement agencies for reports and other documentation are unbelievable in number and scope. This issue has been emphasized in a number of official documents, as in the Staff Report to the Committee on Armed Services of the U.S. Senate entitled "Defense Organization: The Need for Change" published under date of October 16, 1985. The point is also made in a private study entitled The Pentagon and the Art of War by Edward N. Luttwak./1

Finally, in our judgment, there is a central thrust missing in legislating, rule making, and congressional oversight in the defense acquisition area. There are numerous procurement objectives, many of them sound by themselves. However, in many respects these objectives are inconsistent or contradictory when viewed as a whole. Reconciliation of procurement objectives and procedures is seldom attempted either at the congressional or executive branch level. If this situation continues, the result will be very counterproductive.

MAPI appreciates the opportunity to appear in these hearings and stands ready to assist in any other way.

1/ The Pentagon and the Art of War by Edward N. Luttwak, Simon and Schuster, Inc., 1984.

Appendix A

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October 8, 1985

Defense Acquisition Regulatory Council
ATTN: Executive Secretary, DASD (P-DARS)
c/o OUSDRE (MARS) Room 3D139
Pentagon, Washington, D.C. 20301-3062

Dear Sir:

Proposed Defense Department Regulations Concerning Contractor Rights in Technical Data

We wish to comment on the proposed regulatory implementation of the technical data provisions of the Defense Procurement Reform Act of 1984 (Title XII of the Fiscal Year 1985 Defense Authorization Act; P.L. 98-525) and the Small Business and Federal Procurement Competition Enhancement Act of 1984 (P.L. 98-577). Specifically, we address the proposed rule, denominated DAR Case 84-187, published in the Federal Register of September 10, 1985.

So you may understand the great importance of the rights-in-data issue to our membership, we wish to say a word about the Institute. The Machinery and Allied Products Institute (MAPI) is the national spokesman for a wide range of manufacturers and users of capital goods and allied products. In recent years, our membership has been substantially extended beyond manufacturers of traditional capital goods to include producers of electronics, telecommunications products, scientific and industrial instruments, office systems, aerospace equipment, computers, controls, testing equipment, military hardware, and similar high-technology product lines. Although most MAPI member companies are oriented towards commercial rather than government sales, many of them are indispensable to the government's requirements, particularly in national defense and related areas. These companies rely heavily upon continuing technological progress, the bulk of which is developed at the companies' own expense, to produce quality products and maintain their competitiveness. Therefore, they have a vital interest in continued recognition by the government of their proprietary rights in technical data relating to technological developments.

We believe that the proposed regulations do not properly implement the policy requirements of P.L. 98-525 and the proposed Federal Acquisition Regulation (FAR) coverage of technical data/1

1/ A notice of the proposed Federal Acquisition Regulation (FAR) coverage was published in the Federal Register of August 15, 1985. The policy provision is the only portion of the FAR coverage that applies to DOD.

MACHINERY & ALLIED PRODUCTS INSTITUTE AND ITS AFFILIATED ORGANIZATION, COUNCIL FOR TECHNOLOGICAL ADVANCEMENT, ARE ENGAGED IN RESEARCH IN THE ECONOMICS OF CAPITAL GOODS (THE FACILITIES OF PRODUCTION, DISTRIBUTION, TRANSPORTATION, COMMUNICATION AND COMMERCE) IN ADVANCING THE TECHNOLOGY AND FURTHERING THE ECONOMIC PROGRESS OF THE UNITED STATES

because the proposed regulations are unfairly skewed in favor of the government. In fact, unfairness so pervades the regulations that the proposed rule should be withdrawn.

The following are major examples of such unfairness in the proposed regulations:

1. Cap on technical data rights.--P.L. 98-525 (10 U.S.C. 2320(c)) permits DOD to prescribe standards for employing as a negotiation objective the capping of contractors' rights in technical data. The proposed regulations (DOD FAR Supplement 227.473-2(e) and Alternate III to 252.227-7013) do not comply with Section 2320(c) because, while the regulations list four factors to be considered in determining the length of a cap, no factors are prescribed for making the basic determination of whether a cap should be a negotiation objective.

The absence of such standards indicates that DOD may attempt to obtain a contractor's rights in limited-rights data regardless of whether it is cost-effective for the government to do so and whether the data relates to commercial processes or products. In the latter case, there would be an inconsistency with Section 1202(6) of P.L. 98-525 which states that DOD shall "ensure that persons that have developed products or processes offered or to be offered for sale to the public are not required as a condition for the procurement of such products or processes . . ." to relinquish their rights in data relating to such products or processes.

2. Data relating to commercial products and processes.--The proposed regulations (DOD FAR Supplement 227.472(b)) implement Section 1202(6) in an unfairly narrow fashion by adding several requirements which the contractor must meet before DOD is precluded from requiring the relinquishment of data rights in a commercial product as a condition for a procurement. The proposed regulations state that commercial products or processes must be "existing" and sold, licensed or leased in "substantial quantities" at "established catalog or market prices." Further, Section 1202(6) is totally vitiated by the statement in Section 227.472(b) that an offeror's willingness to provide DOD appropriate rights in technical data relating to processes and products sold to the public may be evaluated as part of a source selection.

3. License rights.--The proposed regulations provide for both indirect licensing (DOD FAR Supplement 227.473-2(b) and Alternate IV to 252.227-7013) and direct licensing (DOD FAR Supplement 227.473-2(c) and 252.227-7036) of limited-rights data. The indirect licensing provisions do not appear to fairly protect the interests of the contractor which originated the limited-rights data. Alternate IV to Clause 252.227-7013 states that the government "assumes no liability for use, duplication, or disclosure of such data by others for commercial purposes," yet the proposed regulations do not require that contracting officers require the licensor to sign nondisclosure and non-use agreements that would allow direct enforcement by the originators of the data.

DOD FAR Supplement 227.473-2(c) states that direct licensing ". . . permits contractors to retain direct control over use of their limited and restricted rights data being transferred to the second source." However, this control and enforcement provided the licensor is vitiated by the terms of DOD FAR Supplement 252.227-7036 which states that the government will stipulate desired terms and conditions of any license and will review and approve all direct licensing agreements.

4. Definition of "developed at private expense".—The proposed regulations use the definition of "developed at private expense" as a vehicle for balancing the competing interests of the government and contractors in limited-rights data. However, the proposed regulations do not fairly balance such interests. Further, P.L. 98-525 requires that, in allocating rights in data, the regulations focus on the source of funding, whereas the proposed regulations allocate rights based on the circumstances under which an item, component, process or software package is "developed."

Because of the significance and complexity of the last example above, the remainder of this letter is dedicated to addressing the issues related to the proposed definition of "developed at private expense."

Definition of "Developed at Private Expense"

The Federal Register notice states that the phrase "developed at private expense" has been defined and that the definition establishes the legitimate proprietary interest of the contracting parties as required by P.L. 98-525 (10 U.S.C. 2320). While the proposed definition (found at proposed DOD FAR Supplement 227.471 and 252.227-7013) does establish the proprietary interest of the government and contractors, it does not achieve a fair and reasonable balance between the competing interests of the government and contractors in technical data as required by the conference report on the legislation./1

"Developed at private expense," as defined in the proposed regulations, "means that completed development was accomplished without direct Government payment, at a time when no Government contract required performance of the development effort, and was not developed as a part of performing a Government contract." To be consistent with Section 2320(a)(1) and to fairly balance the interests of the government and contractors in technical data, the preceding definition should end with a period after the word "payment." Without such a truncation of the definition, the government could claim unlimited rights in production processes that were specifically developed by a contractor to reduce its manufacturing costs on a fixed-price contract. Under certain circumstances, the government might also claim unlimited rights to an item that a subcontractor develops at its own expense.

For an item, component, process or computer software to be considered developed at federal expense, not only should the contractor have received direct federal funds, but also the contract should have included a line item requiring the development. This is consistent with the requirement in P.L. 98-525 (10 U.S.C. 2320(b)(4)) that separate contract line items be established for technical data and with the legislative history of the statute.

The legislative history of P.L. 98-525 shows that the conferees felt it was impossible to legislatively establish a balance of the competing interests of the government and contractors in technical data which would apply in all situations, and

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1/ Congressional Record, September 26, 1984, p. H 10303.

therefore they deferred to DOD on the issue./1 In the words of the conferees, ". . . the direction [in 10 U.S.C. 2320(a)] to the Department of Defense . . . to prescribe regulations defining the legitimate interests of the United States and of a contractor to be implemented in the system of government-wide procurement regulations will afford the best opportunity to reach a fair and reasonable balance of these competing interests. . . ."/2 As we indicate below, it seems clear that, despite the mandate from the congressional conferees, no such balance has been struck.

It appears that as part of the decision to allow DOD to draft regulations which would strike a balance in the rights to technical data for all cases, the conferees deleted the definition of "developed at private expense" which was included in the House version of the 1985 Defense Authorization bill (H.R. 5167). That definition, which originally came from H.R. 5064, the "Defense Spare Parts Procurement Reform Act," reads as follows:

> "Developed at private expense", as used in this clause, means with respect to an item (or technical data relating to an item) delivered under a contract, developed without direct payment by the Government under a provision of the contract which requires the performance of the development effort.

The above definition indicates that the House did not intend to change DOD's general policy on technical data because the definition merely recites the broad policy DOD has applied over the past 20 years--that is, only if there is direct payment by the government for the development work is an item, component, or process not to be considered developed "at private expense." It seems clear that the deletion of the House definition indicates only that the conferees felt that it would be better to have that concept drafted administratively by regulation.

Moreover, there is persuasive evidence that at least some DOD policymakers consider the above definition to be the proper reflection of DOD's general policy on technical data. The above legislative definition was adopted in the report, "Who Should Own Data Rights: Government or Industry? Seeking a Balance," submitted to the Under Secretary of Defense for Research and Engineering on June 22, 1984. The report, which was written by the OSD Technical Data Rights Study Group under the direction of Darleen A. Druyun, is referred to hereinafter as the Druyun report. It is apparent that the proposed regulations have adopted portions of the Druyun report.

While the above legislative definition may have been considered to be sufficient for a broad statement of DOD policy on technical data, the conferees apparently felt that a more detailed definition was required. We believe that P.L. 98-525 indicates the nature of the detail that DOD is to provide in its regulations. Specifically, 10 U.S.C. 2320(a) lists the following as one of the factors required to be considered by DOD in prescribing technical data regulations:

> (1) Whether the technical data was developed—
> (A) exclusively with Federal funds;
> (B) exclusively at private expense; or
> (C) in part with Federal funds and in part at private expense.

1/ *Ibid.*
2/ *Ibid.*

However, the proposed regulations do not even address the issue of allocating proprietary interests in technical data developed in part with federal funds and in part with private funds as called for in 10 U.S.C. 2320(a)(1)(C). Whereas Section 2320(a)(1) indicates that the source of funding should be the basis for allocating technical data rights, the proposed regulations emphasize the concept of "developed." "Developed" was not even defined in the above legislative definition of "developed at private expense."

Definition of "Developed"

The proposed regulations define "developed" in the phrase "developed at private expense" in an attempt to further clarify the rights of contractors and government in technical data. Significantly, the definition of "developed" requires an item, component, process or computer software to "have been tested so as to clearly demonstrate that it performs the objective for which it was developed." We believe this definition unduly favors the government and should not be used.

We believe that "workability" is the current standard for determining whether an item, process, component or computer software is "developed."/1 Further, we believe that that standard should be retained because it establishes a fair and reasonable balance between the competing interests of the government and the contractors as required by P.L. 98-525. "Developed," within the concept of "workability," means that "an item, component, process or computer software is considered to be developed if it is brought to a point of development sufficient to demonstrate to one reasonably skilled in the art to which such item, component, process or computer software relates that it performs or can perform the purpose for which it was intended."/2

To "demonstrate" "workability"—

> . . . the item or component must be analyzed and/or tested sufficiently to demonstrate to reasonable persons skilled in the applicable art that there is a high probability the item or component will work as intended. Whether testing is required in addition to analysis, and the degree of testing and whether dynamic as well as static, depends on the nature of the item or component and the state of the art.
>
> * * *
>
> The required analysis and testing need not be enough to bring the item or component to the point where it would be sold or offered for sale if it were a commercial item. Again, further development may be necessary before the item or component would be ready to be sold or offered for sale, and such further development may require validation through further analysis and

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1/ Bell Helicopter Textron, 44 Federal Contracts Report (BNA) 648, 655 (Armed Services Board of Contract Appeals (ASBCA) No. 21192 Sept. 23, 1985).

2/ Ibid., pp. 650 and 655.

> testing. Also, . . . workability, . . . to a high degree of probability, which is enough for an item to be "developed" for data rights purposes, may not be enough to make the item or component ready to be sold or offered for sale; for that, 100 percent certainty would usually be required. . . ./1

As indicated above, the concept of "workability," does not inflexibly require in all cases the testing of an item or component./2 This is consistent with cases under the patent law relating to reduction to practice which have long held that there are items so simple that mere construction alone is all that is necessary to constitute reduction to practice./3

In fact, there may be rare cases where the item, component or process is so simple that its "workability" would be obvious without building a prototype./4 This is consistent with early DOD policy on patent rights./5

Modifications to Items, Components, Processes and Computer Software "Developed at Private Expense"

The proposed definition of "developed at private expense" also addresses the issue of who has rights to the technical data when there is a federally funded modification to an item, component, process or computer software which was originally "developed at private expense." The proposed definition states that in such a case "modification of the item, component, process or computer software shall not be considered to have been developed at private expense." It is not clear from the preceding language whether the entire item, component, process or computer software or only the modified portion thereof would be considered to be developed at federal expense.

Another sentence in the definition of "developed at private expense," however, indicates that the modified portion would be the only part considered to be developed at federal expense. That sentence states that if "the entire item, component, process, or software package was not developed at private expense, separate elements thereof which do meet the criteria will be considered to have been developed at private expense."

It would be manifestly unjust and contrary to current case law if the government were to expropriate a contractor's technical data rights by virtue of a minor modification to an item, component, process or software package which was "developed at private expense." See Patents and Technical Data, Nash and Rawicz, pages 443-45, George Washington University (1983).

1/ Ibid., p. 655.
2/ Ibid.
3/ Patents and Technical Data, Nash and Rawicz, p. 169, George Washington University (1983). See also MAPI's June 14, 1974 letter to Captain Leroy E. Hopkins, U.S. Navy, Chairman of the ASPR Committee, on the "Meaning of 'Developed' in Connection With Limited Rights Data."
4/ Bell Helicopter Textron, 44 Federal Contracts Report, p. 655.
5/ Ibid., p. 654.

Conclusion

We do not believe that the proposed technical data regulations fairly and reasonably balance the government's needs and the contractors' legitimate proprietary interest in technical data as required by P.L. 98-525 (10 U.S.C. 2320(a)) and proposed FAR 27.402, "Policy." While we have noted other problems with the proposed regulations, we are particularly concerned that the proposed definition of "developed at private expense" would significantly and unfairly narrow contractors' rights in technical data and computer software.

As reflected in Section 2320(a)(3) and FAR 27.402, the government has an interest in obtaining rights in data in order to increase competition and lower costs by developing alternative sources of supply and manufacture. On the other hand, Section 2320(a)(4) and FAR 27.402 indicate that contractors' economic position, especially their commercial position, must be protected to encourage qualified contractors to participate in government programs and apply innovative concepts to such programs.

The proposed definition of "developed at private expense" is so skewed in favor of the government that many contractors would be discouraged from participating in government programs and applying innovative concepts. Further, we do not believe that the proposed definition properly reflects congressional intent as manifested by the definition of "developed at private expense" which was included in the House version of the 1985 Defense Authorization bill. The same definition was also included in the Druyun report.

Moreover, we believe that 10 U.S.C. 2320(a)(1) requires DOD to focus, in the technical data regulations, on the issue of the source of funding, not the "development" of an item, component, process or software package. But if "development" is to be emphasized, "workability" should be the standard for determining whether an item, component, process or software package has been "developed."

The proposed definition should be clarified to indicate that a federally-funded minor modification does not give the government unlimited rights in an item, component, process or computer software that was originally "developed at private expense."

Finally, although we have offered these specific suggestions, as indicated at the outset it is MAPI's overall judgment that the proposed regulations are so lacking in balance and fairness that they should be withdrawn.

This concludes our comments on the proposed technical data regulations concerning the term "developed at private expense" in connection with limited-rights data. If we can be of further assistance, please let us know.

Sincerely,

Charles Stewart
President

cc: Dr. James P. Wade
Assistant Secretary of Defense
(Acquisition and Logistics)

Appendix B

MACHINERY and ALLIED PRODUCTS INSTITUTE
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August 8, 1985

General Services Administration
ATTN: FAR Secretariat [VR]
Room 4041
18th and F Streets, N.W.
Washington, D.C. 20405

To Members of the Secretariat:

(FAC 84-10)

Interim Regulations Relating to the
Commercial Pricing Certification Requirement

This is in response to the notice in the *Federal Register* of July 3 requesting comments from interested parties on Federal Acquisition Circular (FAC) 84-10 which took effect on an interim basis on July 3. The Circular has now been reviewed by those companies within the Machinery and Allied Products Institute (MAPI) membership which have a significant stake in government contracting. The discussion and recommendations which follow are based on this review by member companies and on analysis by the MAPI staff.

Specifically, our comments are directed to Item III, Certification of Commercial Pricing, which implemented Section 1216 of Public Law 98-525 (the Defense Procurement Reform Act) and Section 204 of Public Law 98-577 (the Small Business and Federal Procurement Competition Enhancement Act).

Applicability to Spare and Replenishment Parts

Under FAR 15.813-1 as added by FAC 84-10, the new statutory commercial pricing certification requirements have been made applicable to contracts for "items of supply." We think that in view of the legislative history of the statutory requirements, the scope of application of the requirements is too broad. It seems clear from the provisions of the separate House and

MACHINERY & ALLIED PRODUCTS INSTITUTE AND ITS AFFILIATED ORGANIZATION, COUNCIL FOR TECHNOLOGICAL ADVANCEMENT, ARE ENGAGED IN RESEARCH IN THE ECONOMICS OF CAPITAL GOODS (THE FACILITIES OF PRODUCTION, DISTRIBUTION, TRANSPORTATION, COMMUNICATION AND COMMERCE) IN ADVANCING THE TECHNOLOGY AND FURTHERING THE ECONOMIC PROGRESS OF THE UNITED STATES

Senate bills which resulted in the new statutory requirements, that the intendment of the draftsmen of these provisions was to impose a new statutory certification requirement on contracts for the procurement of replenishment and spare parts, rather than on contracts for all items of supply generally.

We acknowledge that the statutes use the broad term "items." But we also note that the Joint Explanatory Statement of the conferees on this provision, after referring to the original provision addressed to "spare or replacement parts" in the House bill, states that "minor clarifying changes" have been made in the original House provision. Under these circumstances and in view of this legislative history, we think it makes more sense to construe the term "items" in the statute as referring to items of spare or replenishment (or replacement) parts rather than to items of supply generally. For that reason, we recommend that, as a matter of administrative discretion, the FAR implementation of the statutory requirement for commercial pricing certification be limited to contracts for spare or replenishment parts.

Application to Contract Types

FAR 15.813-5 provides that the Certification of Commercial Pricing clause should be inserted in all solicitations and contracts "unless exempted under 15.813-3(a) or (b)(1)." FAR 15.813-3 is entitled "Exemptions From Commercial Pricing Certificates." The difficulty here is that FAR 15.813-2, "Applicability," includes a number of criteria, not referenced in FAR 15.813-3, as to when the clause should be used. For example, FAR 15.813-2(1) states that the certificate is to be required in connection with contracts not awarded on the basis of full and open competition. Obviously the reverse of that proposition is important--the certificate is not to be required, and presumably neither should the clause be required, in connection with contracts that are awarded on the basis of full and open competition. In general then, the language included in FAR 15.813-5, relating to when the contract clause is to be used, should be expanded to refer to the criteria included in FAR 15.813-2, "Applicability," as well as the appropriate language in FAR 15.813-3, "Exemptions From Commercial Pricing Certificates."

Recognition of the Role of Original Equipment Manufacturers

The certification of lowest price does not recognize prices to original equipment manufacturers (OEMs) and dealers who add either product or marketing value and resell to end user customers. Such recognition, in our view, is necessary in order to prevent a misunderstanding on the part of those in government who have the responsibility of administering these provisions. Obviously, such sales to OEMs and dealers are sales in which either the items themselves or the circumstances under which they are sold are not comparable to the government sales at issue.

Need for Audit Limitations

Paragraph (b) of the certificate form, prescribed by FAR 52.215-32, gives the contracting officer (or representatives of the contracting officer who are employees of the government) the right "to examine and audit all books, records, documents and other data of the Contractor relating to the pricing of the commercial items covered by this offer/proposal." We think that such audit authority is far broader than is actually needed for the purposes of verifying data provided by the contractor with respect to selling prices in sales of the commercial items in question to other customers. The provision should be revised to specify that the government's audit access is limited to the information that is needed for this purpose, and does not include access to information relating to the costs of producing the commercial items.

Need for Floor on Data

Finally, there is a need to establish a de minimis figure on sales to nongovernment parties and persons that must be taken into consideration in determining whether the government has been offered the lowest commercial price for the item in question. Without such a de minimis amount being specified, we are concerned that the requirement for providing such data with respect to other customers can become a nearly impossible administrative burden.

* * *

This completes our comments on FAC 84-10. If we can be of any further assistance, please let us know.

Cordially,

Charles Stewart
President

Senator QUAYLE. Thank you, Mr. Stewart, for a very comprehensive presentation.

Now I will turn to Mr. Karl Harr, president of the Aerospace Industries Association.

STATEMENT OF KARL HARR, PRESIDENT, AEROSPACE INDUSTRIES ASSOCIATION, ACCOMPANIED BY LEROY J. HAUGH, VICE PRESIDENT, PROCUREMENT AND FINANCE, AEROSPACE INDUSTRIES ASSOCIATION

Mr. HARR. Thank you, Mr. Chairman.

I appreciate also your including my entire statement in the record. I will summarize it, hitting the high points. I will try not to be repetitive of what my two colleagues have said before me.

It is useful, I think, to try to do that because there is so much involved in this massive subject you are investigating here, so many aspects of it that it is hard sometimes to keep the truly important perspectives in mind as we proceed.

I should say that with me is Leroy J. Haugh, vice president, of Procurement and Finance, who works with the laws and regulations on a daily basis.

As far as we are concerned, Mr. Chairman, the work of this subcommittee and these hearings are one of the most important, if not the most important, things we have ever participated in directly.

They are important because the future viability of the procurement process is at stake and, therefore, to a considerable extent the fate of our defense establishment.

It is important because, as General Skantze said to you earlier in this session, the present environment is one of turbulence and trauma.

I think it is important for another reason, too, which I will ask you to think about, and that is that there seems to us to have been a perceptible change in the attitude of the public—effected through the Congress, the public, media—about the defense industry and its place in the American economy and society.

For the roughly 30 years that this industry has existed on a significant scale, it has—because of America's reluctance to have a permanent, enduring peacetime defense establishment—been considered a temporary thing, something that would go away one of these days as soon as the threat was withdrawn.

In the last year or so that has changed. It is now perceived as being here to stay. The public says we do not know quite what you are, but we know you are big, and we know you are here to stay and we had better get about fashioning the rules of the game.

They admit it would not be useful to be nationalized. We are not a utility, we are not captive industry, but they say you are not a normal commerical industry either. That is a different environment that we have existing today.

It points up even more acutely the importance of the work of your subcommittee and the work of the rest of us who are trying to work either in industry or in the Pentagon or in the Congress to come up with some of these right answers.

We are all involved in a major redefinition and restructuring of the procurement process. Some improvements have been achieved. The cost has been great and if not attended to and not monitored and not remedied, we think the costs outweigh the benefits.

Such costs include program administration indigestion from the sheer volume of our laws and regulations; the unwholesome, paralyzing and destructive atmosphere resulting from political and administration pressures based on suspicion; and a loss of potential strength within the process, and from the segments of the process, because of misapplication of principles of authority and responsibility.

I am referring there basically to restricting and hampering and hindering the managerial skills, basically what the Government is buying when it buys weapons systems from us, and impeding the inclusion of technological advances and restriction of our prerogatives.

Everybody says, and we all know it, you preface the hearing on the fact we cannot make final judgments on last year's legislation. We tried to respond to your inquiry with four principles which we believe will serve as a sound guide to an efficient procurement system and against which the merits or demerits of the legislation can be measured.

You have heard a lot about the term micromanagement. We think that is a very, very key element, a fundamental obstacle to putting us on an efficient productive basis. This does not mean reducing oversight. Everybody agrees oversight is both desirable and necessary.

What it means basically is ending a process of having the wrong people making decisions—wrong people in terms of knowledge and responsibility—a process which automatically at the same time relieves the right people—right being defined in terms of knowledge and responsibility—from the responsibility of making those decisions.

Above all, it restricts the flexibility of managerial prerogatives.

Oversight is the Government's prerogative. Management, as long as we here are getting our weapons systems in the private industry, is industry's prerogative.

Those laws or regulations that affect us positively in terms of clarifying it are good laws. Those that obscure it further and make less clear what the responsibilities and duties are are bad.

The second principle is get industry participation at the appropriate time, early in the process of developing procurement policy. How wasteful it is not to use the very important part of the total experience that has been gained in this process and which industry possesses. How wasteful it is to put out policies and regulations, pass laws that as a practical matter are not realistic in terms of how the system works.

Then return to the standard of reasonableness. We have deviated in specific terms from the test of what a prudent businessman would do. The reasonableness test should be once again applied.

Finally, reduce regulations. Every regulation that is unnecessary breeds poison. It is expensive, it is restrictive, it is negative and should be eliminated.

So, as a general guiding principle, reduce regulations to the minimum consistent with getting the job done. We have some examples in our statement of the negative effect of some of the implementations, the area of cost allowability, area of warranties and waivers, the FAR system, and I will be glad to try to answer any questions on those when the time comes.

In sum, as we see it, the situation we are in now is like giving a good team a voluminous and complex play book that no players can or will execute. We say please hold off on any other legislation, if you can.

Please check implementation regularly and make sure it is doing what your prior established legislation calls for.

And finally and most importantly apply to each law and regulation the test of whether it does help delineate clearly the proper lines of responsibility and authority over further abuse.

We in industry will certainly do everything we can to be helpful, Mr. Chairman.

Thank you.

[The prepared statement of Mr. Harr follows:]

PREPARED STATEMENT OF KARL G. HARR, JR., PRESIDENT, AEROSPACE INDUSTRIES ASSOCIATION OF AMERICA, INC.

Mr. Chairman and members of the subcommittee, I am Karl G. Harr, Jr., President of the Aerospace Industries Association. AIA is the national trade association of America's principal manufacturers of commercial, military and business aircraft, aircraft engines, missiles, spacecraft, and related components and equipment.

We are most pleased to respond to your invitation to help review the effect of recent legislation on the defense procurement process.

Given the flood of such legislation over the past three years this review is most appropriate and timely. However, given the relatively short period during which most of this legislation has been in effect, it is premature to pass final judgment at this time. Nevertheless, one thing is readily apparent. Until the massive digestive process required to adapt to and implement all this new legislation is completed, or at least much further along, we certainly don't need more legislation. All of us, the Congress, the procuring agencies and the industry need time to adapt to and examine the effect of what has already been done. This hearing should help toward that end.

Let me say at the outset that I believe we are entering a new phase in the government/industry relationship as it applies to the defense industry. Inherent in the volume of laws and regulations of the past few years is recognition of the fact that our substantial defense industrial establishment is a more or less permanent phenomenon we must learn to live with. Until recently, despite its considerable number of years of existence, the defense industry was generally regarded as a temporary phenomenon which would disappear one of these days when the threat ended. That is no longer the case.

Now the nation seems to be saying, through its media, its Congress and the general public, "We don't know exactly what you are, but we know you are big and you are different and you seem to be here to stay so we better get about working out the rules of the game. It is not desirable that you be nationalized; you are not a public utility; and you are not a captive industry. But you're certainly not the same as a purely commercial industry either."

We in industry are aware of this and what we ask is that, given our experience, we be allowed our appropriate role in establishing the most effective rules of the game.

Thus perhaps the best way for us to respond to the question posed in these hearings is to start with some fundamental principles that we believe are essential to a sound procurement process and try to assess how these principles are affected, pro and con, by this new legislation and the implementing regulations.

AVOID MICROMANAGEMENT

The first principle, and I am sure you have heard much about this, is to do everything possible to avoid micromanagement. This does not mean reducing oversight. Careful oversight is both desirable and necessary. Rather, it means avoiding the negative aspects of having the wrong people (in terms of knowledge and responsibility) make the management decisions and relieving the right people of the authority or responsibility for doing so. Oversight is the province of Congress; management, as long as we adhere to our traditional principles of using the private sector to produce our weapon systems, is the proper province of industry. Laws and regulations which help to simplify and clarify responsibility between the two are good laws. Laws and regulations that complicate or obscure the division of responsibility and authority are bad, and will further impede an already heavily burdened process.

INDUSTRY PARTICIPATION IN DEVELOPING POLICIES AND REGULATIONS

Second, earlier and more meaningful industry participation in the development of policies and regulations, we are convinced, would greatly reduce misconceptions, unrealistic formulations and simple error. Some of the regulations issued now are based on wholly fallacious conceptions of how the process works and how a given regulation will affect the process.

RESTORE THE CONCEPT OF REASONABLENESS IN NEGOTIATING COSTS

Third, we should work to restore the concept of "reasonableness" or "what a prudent businessman would do" in determining allowability of costs. The current atmosphere is demoralizing because it does not permit reasonable difference. The inclusion of any questionable cost leads to charges of fraud or "rip-off." We should together search for greater certainty concerning what is allowable and what is not. Industry has underway a substantial initiative to that end.

But until this problem is solved to the satisfaction of the Congress, the Pentagon, the industry and the public, the atmosphere surrounding the procurement process will continue to be poisoned by suspicion on the one hand and resentment on the other.

The new statutes do not directly address the reasonableness problem but the combined zeal and defensiveness with which they have been implemented tends to have a strong negative effect in that regard. Today, applying a test of reasonableness is a luxury a harried and often nervous contracting officer or auditor feels he can no longer afford.

We should find our way back to that standard of reasonableness.

REDUCE REGULATIONS

Finally, it should be in everyone's interest to reduce rather than to proliferate regulations. Regulations should be kept to the minimum essential to getting the job done. To a large extent, it is the implementing regulations rather than the statutes themselves that are currently giving us the operational problems. That is understandable since it is in such regulations that the rubber meets the road. But it is the tendency to overreach what Congress enacted that is our concern—implementing regulations going far beyond what Congress intended, or revising Congressional intent, or containing inconsistencies and even direct contradictions among the Services.

We are experiencing some dangerous trends in this respect which, if allowed to continue, threaten the viability of the industry and of the procurement process. There is a slow-down in the process, almost to the point of paralysis in many cases. The statutes do not require or even suggest the level of "super caution" that exists. Nevertheless, they have resulted in an atmosphere of one-upmanship in which judgment, responsibility and accountability are ignored. Contracting officers are often afraid to make judgments or decisions that will almost surely be second-guessed later. Procuring activities are concerned that their actions will be criticized at bureau, command or agency level. And so on up the line. No one wants to take an action that could be viewed as "soft" on industry. The result is a sharpened adversary relationship that tends to be neither productive nor healthy.

Mr. Chairman, I don't for a minute suggest that there are not problems that need to be corrected. But I do believe the perceived problems are so magnified by the press, Congressional hearings, GAO reports, IG reports and so forth as to produce an overreaction which doesn't just ripple throughout the system, it floods the system.

We do not castigate DoD or the Services for this. They are trying the best they can to get on top of their monumental task. But as they admit, confronted with the huge volume of new law, in some cases containing radical departures from prior practice—and confronted with the manifest Congressional desire for rapid and thorough implementation—their efforts to give effect to the will of Congress have produced considerable turmoil.

The DoD regulation drafters are not people of ill-will or incompetence. To the contrary, the procurement professionals of DoD include many of the best. They are, however, under such pressures of time and politics that they are almost unable to proceed at all. Many of the people in the field fear the reaction of Congress and the press if warranty requirements are waived. They often seem to have become so immersed in the process of their deliberations that their substantive goal has been obscured.

For whatever reason, we think that in many cases the implementers have gone too far. Out of zeal to show their good faith to Congress, out of an excess of caution to forestall subsequent criticism, out of simple misunderstanding, or whatever, regulations have been promulgated that in some instances clearly go way beyond what Congress intended, or even frustrate that intent.

Let me give just a few examples to illustrate my premise.

COST ALLOWABILITY

Throughout the authorization and appropriations process this year, Congress has considered and passed a wide variety of changes to the types of costs allowable under defense contracts and the means of resolving differences over them. DoD, in some cases, has tried to anticipate Congress' desires by issuing major changes on its own, like the overhead cost certification directive. In the eight months since that directive was issued, DoD has found it necessary to issue a series of "clarifications"; Congress has acted to codify it once; and Congress is now considering a second statute to change the first. It is the same in other cases. DoD hastily drafts regulations to meet tight statutory implementation dates. Often because of the pressure of time, field implementation of the new regulations is left up to the Services, and each Service, even each buying activity, frequently ends up doing things its own way.

WARRANTIES ARE BEING REQUIRED WITHOUT REGARD TO TECHNICAL RISK OR COST

When Congress passed a requirement for performance warranties on major weapon systems last year, it set up two business decisions for DoD to make as a precondition to its application. First, are the weapon systems in "mature, full scale production" so that technical risks have been reduced to the point that warranty liabilities can be assessed? Some of our companies advise us that warranties are being required well short of mature full scale production. The second precondition is whether the warranty will be cost-effective. Where they are not cost-effective, DoD could waive the requirement and report the waiver to Congress.

Last year Congress said that a failure to conduct cost-benefit analyses and to process waivers would defeat the legislative intent. It provided flexibility in making the warranty decision to guard against this. Yet in the year since the warranty mandate was clarified, DoD has sought only one waiver of it. Should this not raise a red flag for Congress, warning that cost effectiveness decisions are not being made in the manner intended? We are concerned that in too many cases warranties are being required because of fear of criticism should a procuring activity attempt to obtain a waiver.

RIGHTS IN TECHNICAL DATA

The Defense Procurement Reform Act and the later Small Business Competition Enhancement Act sought to increase competition for spare parts orders by expanding the Government's rights in technical data. This legislation was enacted at the height of the disclosures regarding allegedly overpriced parts. Nevertheless, Congress clearly stated its concern that there be a balancing of interests. The government's need for data should be balanced against the contractor's legitimate proprietary interests in data developed at the contractor's private expense. We do not question the Government's need for rights in technical data when necessary to its mission. However, the concept of balancing of interests appears to have been overlooked in the early attempts to implement the data rights provision of the statutes. DoD has issued temporary regulations to comply with the statutory deadline, and extended the public comment period to January 9, 1986, on its proposed final regulations. We are hopeful that we will be able to reach agreement on some mutually acceptable regulations by the end of this period but, at the moment, we are literally miles apart. The proposed DoD regulations go far beyond the statutory intent, far beyond what is needed to solve the spare parts problem, and would certainly add significant cost to the government.

Here again, I do not want to suggest that there is not a spare parts problem. But I am concerned that too few people understand the complexities of spare parts procurement. The solution to whatever problems exist is not the wholesale acquisition of more data. DoD must first develop a good system for effectively managing data, and then make judicious determinations as to what data is required for competitive reprocurements. And, equally important, DoD must recognize and respect a contractor's legitimate proprietary interests in data the contractor has developed at his own private expense.

FAILURE TO ADHERE TO FEDERAL ACQUISITION REGULATIONS SYSTEM

When Congress reauthorized the Office of Federal Procurement Policy in 1983, it mandated a uniform, government-wide Federal Acquisition Regulation (FAR) System. Variations by the agencies were supposed to be limited to: (1) directives essential to implementing the government-wide system within the agency; (2) regulations essential to specific and unique needs of the agency. The recent legislation, much of it directed solely to DoD, has made adherence to a single regulation difficult at best. Add to this the tight statutory deadlines and the propensity to over-implement for fear of being branded as soft on industry, and we are faced with a proliferation of regulations and "memo" regulations which threatens to destroy the FAR concept.

When Congress created the Federal Acquisition Regulation to be a government-wide uniform procedure for contracting, it assumed that further refinements of the statutory underpinnings could be smoothly worked into it. The flood of legislation in the past two years has proven that theory wrong. Warranties, rights in technical data, and the other areas mentioned here are only a few highly visible examples of the more than 150 issues waiting to be resolved by the committees drafting the regulations. The net result of this wave of reform is frustration. Frustration in an industry which cannot determine the ground rules and frustration in DoD, which has been unable to work the changes into an already complex system.

Congress and the American people expect things to work. But the continued insistent calls for correction are slowing the procurement process to the point where it will not be able to accomplish anything. We are reaching regulatory and procedural gridlock.

The inconsistencies among the Services truly create a confusing hodgepodge for industry to deal with. Since it is obvious that most of these regulations would not be issued without the underlying statute, to that extent we are inferentially criticizing the volume and pace at which such legislation has been enacted. Incidentally, the pace is such that Congress sometimes finds itself holding legislative hearings after the legislation has been passed.

WHAT NEEDS TO BE DONE

Existing legislation is a fait accompli and while much of it we would not have originally supported, we believe we can live with it if implementing regulations preserve Congressional intent and are developed in a sensible, orderly and consistent manner. Right now we are approaching chaos in this regard and unless that condition is quickly resolved the costs to all concerned—and to the nation—will be high indeed.

More and more, well-intentioned measures have intruded on the management of defense contractors' business. Corporate risk assessment, audit management, and even attendance at negotiations of contracts or settlements are now directly governed by legislation emanating from a dozen Congressional committees. Less and less flexibility is left to DoD and industry.

By continuing this trend, Congress is taking away the best means of ensuring that the nation gets the latest technologies and the most for every dollar spent on defense. In fact, it is taking away one of the principal assets it is paying for—the managerial capability of its suppliers.

Congress should step back and look at what it has accomplished over the past few years. Major strides have been taken to solve the issues of spare parts pricing, inadequate competition, allowable costs, and other perceived problems. Additional legislation is not needed; regulations which go beyond the intent of the existing legislation defeat the intent of Congress and are counterproductive.

So our message would be: (1) as little as possible new procurement legislation for the time being, please; (2) check those implementing regulations periodically to be sure they're carrying out your will; and (3) above all subject them to the test of whether they clarify or obscure the proper roles and functions of the various parties to the procurement system.

We have many specific recommendations dealing with improving the procurement process which are not appropriately included in the scope of this hearing—but we are firmly convinced that a system that adheres as closely as possible to the fundamental principles discussed above cannot go too far wrong.

In conclusion, yes, it does seem that the defense industry is here to stay for a more or less indefinite period; and yes, as that fact is being recognized, it does seem timely and appropriate to set about defining the ground rules that shall prevail. We have all learned a lot about what works and what doesn't work through our experience in procurement activities of the past thirty years.

Much of that experience necessarily has been gained by industry. We hope that the government, both Congress and DoD, will avail themselves of such knowledge as they proceed. We shall certainly do everything to be helpful.

Thank you very much.

Senator **Quayle**. Thank you very much, Mr. Harr.

The final witness is Mr. Vico Henriques who is the President of Computer and Business Equipment Manufacturers Association.

STATEMENT OF VICO HENRIQUES, PRESIDENT, COMPUTER AND BUSINESS EQUIPMENT MANUFACTURERS ASSOCIATION

Mr. **Henriques**. Thank you, Mr. Chairman.

My statement is complementary to the statements of Messrs. Rittenhouse, Stewart, and Harr, so I will summarize and leave to you and your staff the reading of the entire statement.

Senator **Quayle**. Your entire statement will be made a part of the record.

Mr. **Henriques**. Improvement of the procurement practices is an important, worthy goal and we heartily support, as an industry and as taxpayers, the continued congressional interest in Government procurement.

We have worked hard, and, I believe, well with you and your staffs to respond to the problems and to achieve a more equitable procurement system for commercial products. That system allows the Government to procure commercial products efficiently at firm, fixed prices with selection based on the lowest total life cycle cost solution to the Government's requirement.

I take a moment simply to commend you, Mr. Chairman, and particularly to commend your staff on the work they have done with us and for the help that they have provided to us in looking at Federal Acquisition Circular 84-10 and assisting in the structure of the dialogue between us and the Department of Defense.

I think it is important to point out, however, that there is a significant difference between cost-based and commercial products. I would refer back to Mr. Rittenhouse's statement in the beginning when he described the industry that is particularly responsive to Government-specified and Government-designed products and contrast that with commercial products.

In the unique product business, Government funds the development, design and manufacture of the product. The Government stands many, if not all, of the risks. The Government is the sole purchaser; therefore, the Government must pay for all the costs associated with what is in effect a custom designed and manufactured product.

In commercial product business, on the other hand, research, development and manufacture are the risk of and at the expense of private investment. The company stands the risk, not the customer. There is a very broad public market. Prices are set by the buying public in this marketplace and the Government is only one participant in that market, a significant participant, but certainly not the dominant one.

I would like to make very clear the fact that any manager in the commercial business who consistently fails to price commercial products high enough to recoup the cost of running the company will eventually lead that company into bankruptcy.

Equally, the manager who prices a product too high will find no market for the product and, again, will find his company in economic distress. In our industry the commercial system works to produce highly competitive products at low prices.

Government and, in the context of this hearing, DOD, have long since recognized that it can save taxpayers' money by buying commercial products whenever possible rather than by having all products specifically designed to be produced for the Government.

The 1984 Competition in Contracting Act, for instance, clearly recognized the value of the commercial system by designating the commercially based Multiple Award Program as a competitive means of procurement.

During congressional consideration of the two bills dealing with procurement reforms specifically related to DOD, it appeared to us that the focus of Congress was not upon widely marketed high technology commercial products, such as those of our industry, nor on companies who are the manufacturers and regular dealers in such products.

We are concerned now that DOD is blurring the lines between commercial and cost-based products. The two examples I would like to point out today are the Federal Acquistion Circular 84-10 (FAC 84-10) and the Technical Data Rights regulation. Both of these implement the Defense Procurement Reform Act of 1984 and the Small Business and Federal Procurement Competition Enhancement Act of 1984.

I will not go into any details specifically here because I laid them out in my statement, but I call them to your attention because they are illustrative of two serious, but easily remedied problems that we are having with the implementation of the 1984 procurement laws.

First, DOD is painting commercial products and cost-based products with the same brush. This has caused them to do things like demanding access to all information pertaining to our costs, as in FAC 84-10, which for a commercial product is really none of DOD's business.

Second, and contrary to what I believe was the Congress' intention, these regulations were published with little or no opportunity for industry to comment. There was no dialog between industry and Government. Therefore, we were unable to warn DOD in advance that they were proposing an unworkable set of regulations in the commercial product area.

Furthermore, as Mr. Rittenhouse pointed out, OMB has agreed with many of our concerns on FAC 84-10 and has disapproved it because:

> No justification has been provided for requiring vendors to justify their lowest price charged to any customers when the statute calls for comparison with the lowest commercial price.

Quoting again:

> The practical utility of acquiring data about how prices for commercial items are developed has not been shown.

Also, DOD has realized that their proposed industry rights regulations were in serious need for further industry comment. They have decided to go forward with minimum rule changes to meet the statutory requirements for now and have extended the comments period for these detailed and, in our view, flawed proposed rules another 3 months.

In sum, I think, Mr. Chairman, we would suggest two fairly simple remedies to prevent this kind of thing from happening in the future.

First, in any future procurement legislation you can make clear to the regulating agencies that there is a fundamental difference between commercial and cost-based products and, therefore, they must be treated differently.

Second, you can mandate an equitable and open rulemaking process.

I will be happy to answer any questions you may have, Mr. Chairman. That concludes my statement.

Thank you.

[The prepared statement of Mr. Henriques follows:]

TESTIMONY OF THE COMPUTER AND BUSINESS EQUIPMENT MANUFACTURERS ASSOCIATION

I am Vico Henriques, president of the Computer and Business Equipment Manufacturers Association (CBEMA). I want to thank you very much for inviting me here to discuss with you the problems my industry is having with the current implementation of recent Congressional procurement law revisions. In particular, I would like to discuss the need for a dialogue between our industry and the Department of Defense (DOD) through which a number of issues could be resolved to prevent the implementation of inappropriate and counter-productive regulations.

CBEMA is the trade association of producers of information processing, business and communications products, supplies and services. Its 39 member companies had combined sales of more than $135 billion in 1984. They employ more than 1.6 million people worldwide. In addition, we consistently contribute a positive balance of trade to the national average.

Improvement of procurement practices is an important and worthy goal. We heartily support, as an industry and as taxpayers, the continued Congressional interest in Government procurement. We have worked hard and, I believe, well with you and your staffs to respond to problems and to achieve a more equitable procurement system for commercial products. That system allows the Government to procure commercial products efficiently, at firm fixed prices, with selection based upon the lowest total-life-cycle-cost solution to the Government's requirements.

In its procurement legislation, Congress has continually urged implementing departments such as Defense to open dialogues with industry prior to the implementation of regulations. You recognized, as do we, that in-depth discussion of complex issues must precede the implementation of fair rules that benefit the taxpayer and industry alike.

Unfortunately, that dialogue has not occurred in the implementation of the procurement reform legislation of the 98th Congress. The result has been a series of regulations that confuse cost-based procurement actions with fixed-price commercial procurement. Industry simply cannot concur in this confusion. And the results, should the confusion continue, will be detrimental to the commercial product industry, the Government, and the taxpayer.

There is a significant difference between cost-based and commercial fixed-price procurement. In cost-based procurement, the Government contracts with a vendor for the development and manufacture of a Government-designed, or -specified unique product. Prices for these unique products are based on the costs directly attributable to developing and manufacturing the product as well as an appropriate share of indirect costs, including overhead. Because anticipated profits are negotiated on the basis of a percentage of anticipated costs, the Government has a need to examine all elements of cost to prevent profiteering at taxpayer expense.

In commercial procurement, the Goverment acquires commercial products from vendors at market or discounted prices. The prices of commercial products are determined quite differently from those developed under cost-based procurements. They are not based simply on the cost of developing and manufacturing a particular product. They are based on a highly competitive commercial marketplace which determines what is a fair price. This price must include a contribution to the costs of running the company, to the research and development of new products, to the training and retraining of employees, and, hopefully, to the profits of the company.

Let me make this clear. Any manager who consistently fails to price commercial products high enough to recoup the costs of running a company will eventually lead that company into bankruptcy. Equally, the manager who prices a product too high will find no market for the product.

In our industry, the commercial system works to produce highly competitive products at low prices. Government has long since recognized that it can save taxpayer money by buying commercial products whenever possible, rather than by having all products specifically designed and produced for Government. The 1984 Competition in Contracting Act, for instance, clearly recognized the value of a commercial system by designating the commercial-based Multiple Award Schedule program as a competitive means of procurement.

In our industry in particular, Government has benefited from the tremendous leaps we have made in the relationship of price to performance. The commercial marketplace has been highly competitive, driving down prices and at the same time driving up performance and quality. Thus, commercial procurements are clearly in Government's best interest. They are good for the country, good for the taxpayer, good for business and good for the national defense.

Unfortunately, we see today a growing confusion, a blurring in the minds of some regulators between procurement policies appropriate for cost-based products on the one hand and for commercial products on the other. We see a counter-productive move toward a system in which the contracting concepts for unique, cost-based products are more frequently applied to the acquisition of commercial products and services.

Over the past two years, we have seen some clear problems in the cost-based procurement area and in procurements in which cost-based contractors are allowed to buy commercial items connected with a unique system and then add on overhead to the commercial price. Thus we have notorious cases like the $7 hammer that cost Government over $400.

But these situations do not stem from the procurement of commercial products. Regulations therefore should not be aimed at the commercial marketplace. Unfortunately, because of the regulators' confusion of unique products with commercial products, they are attempting to apply one set of principles to two significantly different categories of vendors.

Two examples of this highly undesirable evolution are: Federal Acquisition Circular (FAC) 84-10 -- Item II (Integrity of Unit Prices) and Item III (Certification of Commercial Pricing)-- and the technical data rights regulations. Both of these regulations implement changes enacted by the Defense Procurement Reform Act of 1984.

FAC 84-10 results from provisions of the Defense Procurement Reform Act which, a review of the legislative history shows, were aimed at the spare parts "horror" stories of the last few years. The objective of these provisions was to eliminate alleged overcharging by defense prime contractors for spare parts, primarily in defense weapons system procurement. Indeed, in the October 29, 1985, hearing of this Subcommittee, some of the joint logistics commanders testified that such spare parts overcharging horror cases were limited to Air Force aircraft procurements. The Congress outlined two primary causes for such overcharging:

1. The grossly unjustified allocation of overhead costs by prime contractors to spare parts which the prime did not manufacture but procured from a subcontractor. The problem was not the price which the prime paid for the part, but rather the allocation by the prime of very high overhead costs which were completely out of proportion to the price the prime paid for the part; and

2. Questionable prices charged to DOD for spare and replenishment parts where the defense contractor was the sole source of supply. Questions were often raised as to the true proprietary nature of the part and/or the existence of a valid commercial market for the part.

Please note that the focus of Congress was not upon widely marketed high tech commercial products, such as those of our industry, nor upon companies which are the manufacturers of or regular dealers in such products.

Mr. Chairman, I'm sure you and the Subcommittee members will recall that a number of the legislative initiatives on both sides of the Congress that ultimately resulted in the relevant provisions of the law clearly were intended for spare and replacement parts. In fact, even as the two versions of the bill were going into conference, the pertinent sections related to Item III of FAC 84-10 were clearly limited to commercial pricing of spare parts. The commercial products industry was startled by the product of the House-Senate Conference which used the much more expansive words "Commercial Pricing for Supplies" and "items" or "items or supply." While this expanded wording concerned us, we concluded that:

a. The legislation was beyond the point of change, but we believed the legislative history would support limiting its application to spare parts; and

b. We could live with the provisions since the statute limited the scope to lowest commercial price in similar circumstances as the Government contract. We viewed this as including both similar terms and conditions of sale and similar class of customer. Furthermore, the provisions only applied to contracts entered into using other than competitive procedures.

However, when FAC 84-10 was issued on July 3, 1985, we discovered that the Federal Acquisition Regulation (FAR) Councils had greatly expanded the scope of the statute and had developed regulations which applied cost-based procurement policies and procedures to commercial product manufacturers. In truth, what had started as a legislative effort to fix spare parts procurement from defense prime contractors, under cost-based contracting, had instead resulted in regulatory overreach that swept in commercial product manufacturers. Furthermore, it did so in a fashion that would violate the propriety of commercial product information and cause such companies to significantly alter their normal business practices and management systems if they wished to sell valid commercial products to the Government.

The most disturbing aspects of FAC 84-10 are:

- The certification of commercial pricing is not limited to the statutory provision of lowest commercial price in similar circumstances. Rather, it was greatly expanded to include:
  - Governmental as well as commercial customers
  - International as well as domestic sales
  - Intra-company transfers as well as external sales
  - Original equipment manufacturers (OEM), dealers, and remarketers as well as end-user customers (the latter being the Government's classification)

- The contracting officer is authorized to require commercial pricing certificates even when full and open competition exists. This clearly is:

  1. A significant expansion beyond the statute's intent to limit the application to situations using "other than competitive procedures."

  2. Contrary to some of the basic principles of competition established in the Competition in Contracting Act; and

  3. An undercutting of the commonly accepted methodology of lowest total-life-cycle-cost selection. This methodology is widely used in high-tech commercial product procurement and has been required for Defense ADP procurement by the House Appropriations Committee.

- A contracting officer may audit all books, records, documents, and other data related to the pricing of commercial items. This is information that is extremely sensitive and proprietary in commercial product companies. It is the type of information the Government would have when it funds the development of a unique product under a cost-based governmental contract. However, we strongly feel that the Government has no right to such information when it merely buys a commercial product which has been developed at private expense.

- Recordkeeping requirements to support these inappropriate audit rights go far beyond normal commercial product recordkeeping; they would extend to three years beyond the last payment on the Government contract. This period might extend for 10 or 15 years or longer on some contracts. This again stems from cost-based procurement policy.

We have similar problems with Item II of FAC 84-10 -- Integrity of Unit Prices. This item implements the desire of Congress to fix the inappropriate overhead allocation by prime contractors to products they do not manufacture, but acquire from subcontractors. Item II does this by requiring that:

(1) Any proposal submitted for the negotiations of prices for items of supply shall distribute costs within contracts on a basis that ensures that unit prices are in proportion to the item's base cost (e.g., manufacturing or acquisition cost), and

(2) The offeror/contractor shall also identify those supplies which it will not manufacture or to which it will not contribute significant value.

The overhead allocation problem does not exist in commercial products at the manufacturer or regular dealer level (whether they are sold to the Government directly or through a prime contractor). These prices are not based upon a build-up of costs under a Government contract, but rather upon the competitive forces of the commercial product marketplace. Therefore, the requirements of paragraph (1) are not applicable to prices of commercial items at the manufacturer or regular dealer level. Thus the identification requirement of paragraph (2) to in effect trigger paragraph (1), is unnecessary and inappropriate at that level. Clearly the sale of commercial items, either to the Government directly or to a Government prime, by such manufacturers or regular dealers should be exempted from the provisions of Item II. Item II would still properly apply to the actions of a non-manufacturer/regular dealer prime contractor after it acquires the commercial item from a manufacturer or regular dealer.

This would be consistent with Congressional intent. It is clear to us, and we submit clear to the authors of the legislation, that the problem did not lie with the manufacturer or dealer of the "$7 hammer." Yet, without an exemption, the impact of the implementing regulation would reach the commercial hammer supplier.

As a result of the numerous written public comments, oral discussions at a public meeting held on September 10, 1985, and other "after the fact" industry/Government dialogues, we understand that some of our problems with FAC 84-10 will be eliminated or reduced when final regulations are issued. However, we do not presently expect this to be the case in a number of Item III areas such as: the inclusion of Federal agencies in the price comparison; the use of certification despite full and open competition; the application of the certificate to devices, rather than only spare parts; and the failure to recognize that the Government is an end-user for purposes of comparison and certification. In addition, there is the wrongful coverage of commercial product manufacturers and dealers under Item II.

We also anticipate that the final rule will contain an illogical expansion that was not present in the FAC as published, but which appeared in a September 4, 1985, redraft. That is the application of the requirement of commercial pricing certificates to sealed bid acquisitions. This makes no sense since sealed bid acquisitions by their very nature are price-based competitions. We suggest that our experiences with FAC 84-10 should cause the Congress to look into this tendency for significant regulatory expansion.

We appreciate any help the Subcommittee can provide in minimizing the unwarranted impact upon our industry of the final regulations which have yet to be issued. We also request you consider the inadvertent impact of legislative and regulatory reforms aimed at cost-based defense contractor procurement upon the commercial product industry.

Industry disagreement with the substance is only part of the FAC 84-10 problem. A second part of the issue is that the regulation was implemented with no opportunity to discuss or comment. Instead, industry was expected to comply instantly when the regulation was issued, with no discussion and no recourse. The information which FAC 84-10 requires of industry is simply not available because it is not needed for the vendor's normal internal business purposes and the systems necessary to collect it will be very costly to develop and maintain.

Furthermore, the Government does not propose to reimburse commercial product producers for their costs of compliance with the regulations. Yet, we must recover those costs in some way. The net effect will be to make U.S. commercial products more expensive for all of our customers and less competitive in the international marketplace.

Had there been a DOD/industry dialogue prior to the implementation of FAC 84-10, I have every confidence that reasonable people could have arrived at reasonable accommodations, but the 30-day period in which to comment followed implementation. We were expected to comply with a regulation that strikes at the very root of the commercial procurement system while we were devoting a very significant effort to analysis and writing, in an attempt to get the regulation modified. I suggest that steps must be taken to bring industry into the procurement rulemaking process much earlier and in a much more cooperative fashion than has been done to date. Since in the case of FAC 84-10, the waiver authority of Section 22 of the Office of Federal Procurement Policy (OFPP) Act was used to avert the normal rulemaking process, the Subcommittee may wish to reexamine the provisions of this waiver authority. This waiver authority seems completely inappropriate for regulations expanding significantly upon statutory language and Congressional intent.

A second example in which the confusion between unique and commercial products has led to tremendous problems is our experience with the implementation of technical data rights regulations.

As background of this problem, DOD was trying to reduce costs for spare parts for unique products. In the past, these parts frequently have had to be bought from the original vendor, often at prices Government considered too high. It was alleged that one of the reasons for these sole-source situations was that the original vendor held the necessary rights in technical data needed to procure the item.

There was an effort by the Air Force and Navy to ensure the Government would have the rights to technical data and could pass them on to other vendors who could, in turn, produce more reasonably-priced spare parts. Unfortunately, the rights to commercial and unique products were comingled, even though the original problem had nothing to do with the commercial marketplace.

As directed in the Defense Procurement Reform Act of 1984, DOD was given one year to implement the provisions of this statute regarding rights in technical data and computer software. Because these regulations would have a major impact on the manufacturers of commercial computers and other high-technology office equipment, it was very important to the CBEMA member companies to work the issues early in cooperation with the FAR Councils, to ensure that the regulations fairly and equitably recognized the rights of commercial vendors, as well as the needs of the agencies.

For months, our industry pursued a dialogue with DOD on the technical rights issue, to no avail. Finally we were faced with a very complex set of regulations with a mere 30-day comment period. DOD announced in advance that the final regulations would be issued two weeks after the close of the comment period. It seemed unlikely that industry views were going to be given serious consideration.

The regulations have serious shortcomings and fail to meet even the most basic expections of our industry. In addition, the Defense Supplement is not congruent with the parent regulation, FAR Part 27.4, which also was published on short notice with major issues not resolved.

In the CBEMA comments submitted to the FAR Council on September 30, we point out the absence of many definitions, which are crucial to the orderly interpretation of the regulations. Without proper definitions of the many vague or undefined terms, it is not possible to use the parent regulation, much less the DOD Supplement, to reach equitable agreements on data right issues.

Also, the DOD regulations are clearly skewed in favor of poorly defined "needs" of the Government. The need for contractors to preserve their commercial markets for privately developed items should be clearly stated in the policy, with an injunction against destroying proprietary data rights for privately developed items, when other measures, such as direct licensing, will satisfy the Government's minimum needs. The language in the laws regarding privately held rights are correctly stated in the regulation but are quickly followed by modifiers that convey a strong preference for acquisition of unlimited rights.

Finally, CBEMA does not believe that DOD has met the intent of P.L.98-525 regarding the expiration of limited rights after a period of time specified in the contract. The law instructs the Secretary of Defense to "prescribe standards" to determine under what circumstances it shall be necessary to acquire unlimited rights after a period of time specified in the contract. Such written instructions should include, for example, a requirement that the contracting officer document why licensing and other options were not feasible before attempting to negotiate a time-limit for limited rights.

Fortunately, DOD ultimately recognized that their proposals were unworkable. They made minimal changes to the existing regulations and issued them as an interim regulation to comply with the mandated timetable. At the same time, they set January 9, 1986, as the close of the comment period. We hope that this new spirit will allow us to work closely with DOD to ensure that these final regulations meet the expectations of both industry and the DOD users who depend on high-technology commercial products and services.

I've given you two examples of ways in which Government's refusal to engage in a dialogue with industry is leading procurement regulation seriously awry. But FAC 84-10 and the technical data rights issues are just examples. There is, in fact, a general drift, a general evolution toward a procurement system that seems to deny the differences between the unique and commercial marketplaces. This evolution is occurring without a meaningful dialogue with industry about the confusion.

Our industry is fighting what often seems to us to be a losing battle with Government over commercial product procurement. Regulations seem to be stepping away from concepts like pricing based on the lowest total overall costs of products. Regulations seem to be de-emphasizing quality function and productivy and stressing instead lowest possible price. Regulations seem to be abandoning the idea that Government seeks the lowest price that competition can reasonably produce, and replacing it with the concept that Government has a right to dictate commercial prices or gain access to the commercial supplier's costs.

Right now, our industry is absorbing tremendous blows. But the ultimate loser will be Government and the taxpayer. The commercial marketplace will not be able to absorb these new Governmental demands under its current price structure. It may gradually be forced to scale back its dealings with Government. In turn, Government will have to increase its reliance on costly unique products. Further, and to the ultimate detriment of the U.S. national strength, our industry will be internationally non-competitive.

Happily, this scenario is not inevitable. You can prevent it. You have the power to stop this trend toward using the same rules to procure unique and commercial products. We see a need for clarifying legislation. For example, you could specify distinctions between the two types of products in your legislation. And you could direct the regulation writers to enter into meaningful dialogue with industry at the earliest opportunity after legislation is enacted so that both sides can better understand the other's objectives, problems and capabilities. Such cooperative dialogue could go a long way toward avoiding the confrontational environment that has enshrouded Government procurement in the past year. Ultimately, dialogue could serve to benefit both the taxpayer and the nation.

I have spoken here today only in general terms. I would like to offer for the record our detailed comments submitted to the FAR Councils on FAC 84-10 and technical data rights. In addition, I would be happy to provide answers to any of your questions.

CBEMA

August 9, 1985

General Services Administration
ATTN: FAR Secretariat (VR)
Room 4041
18th & F Streets, N.W.
Washington, DC 20405

SUBJECT: Temporary Regulation Federal Acquisition
Circular (FAC) 84-10

Dear Sir:

This letter is submitted in response to the notice and request for comments that appeared in the July 3, 1985 Federal Register, Volume 50, pages 27560 through 27563 and corrected in 50 FR 28103 dated July 10, 1985.

In another CBEMA letter, also dated August 9, 1985, we indicate that by separate letter CBEMA would comment on Item II of the FAC 84-10, "Integrity of Unit Prices." The digest of legislative history contained in Enclosure I of the other CBEMA letter covered both Item II and Item III, "Certification of Commercial Pricing." A copy of that enclosure is appended for your ready reference and convenience.

Item II of FAC 84-10 references section 1245 of P.L. 98-525, which is entitled "Regulations for allocating overhead to parts to which the prime contractor has added little value." CBEMA wishes to make the following comments about Item II:

Comments as to Item II--Integrity of Unit Prices

(FAR 15.812-1 & 2 and FAR 52.215-26)

1. It is evident from the legislative history that Congress was concerned with unreasonable overhead costs being applied to spare or replacement parts. The FAR sections, as drafted, are too broad in their thrust. To place the implementing regulations in proper focus and context, certain definitions are necessary. CBEMA's redraft of the material (see Enclosure II) provides the requisite definitions.

2. By the words of section 1245, the implementing language should address procurements that utilize "other than competitive procedures," as that term is defined in the Office of Federal Procurement Policy (OFPP) Act. Referring to the OFPP Act, "competitive procedures" is defined as utilizing procedures that lead to an award through full and open competition. Consequently, section 1245 was only addressing procurement actions that were placed without full and open competition. Both the text of 15.812-1(b) and 15.812-2 overreach; they seek information from the offeror/contractor in settings where, by statutory definition, full and open competition exists. Moreover,

Congress did not superimpose the "adequate price competition" test from P.L. 87-653 as an additional, qualifying burden that the contractor must meet in order to escape the information requirement of Section 1245. Again, these sections plus the implementing clause have been redrafted to confine it only to the correct criteria, i.e., absence of full and open competition.

3. The information sought from the offeror/contractor is totally inappropriate when the vendor is either the manufacturer or a regular dealer who sells items (e.g., parts) through established commercial channels. Referring to the legislative history (see Enclosure I), Rep. Bedell was not addressing the commercial product manufacturer or dealer when he introduced his proposed section 2321 so as to "eliminate the ways the contractor justified $435 for a $7 hammer." In addition, the conference report comments (pages 326 and 327) accompanying section 1245 are instructive. In deferring to the DOD administrative process (rather than passing detailed legislation), the conferees stated:

> "The conferees recommend that the Department of Defense review alternate pricing methods, including (1) allocation of overhead and administrative expenses according to the value of an item and (2) separate pricing of support services provided by prime contractors." (emphasis added)

These recommendations, plus the comments in the conference report preceding the quotation, make it very clear that Congress was not addressing the purchase of commercial items from normal channels of supply (manufacturers, etc.). The FAR Council in its draft has gone beyond the problem at hand, with the result that it places needless burdens on the commercial item supplier. Our redrafted version corrects this matter while still requiring a prime contractor to distribute costs in a manner that does not distort unit prices when the prime acquires a commercial product from a third party and incorporates it into his Government contract.

4. The two statutory provisions (section 1245 plus section 501 of P.L. 98-577) do not require a "pass-on" of its requirements below the prime contractor; however, the FAR clause 52.215-26 in its subparagraph requires its inclusion in "all subcontracts." Clearly, Congress was focusing on prime contractor pricing and overhead allocation practices, as the earlier quotation indicates. Moreover, unlike other legislative enactments (e.g., P.L. 87-653) which specifically refer to "subcontractors" as being encompassed by the legislation, the two aforementioned sections are silent. The legislative history, coupled

with the two sections' reference to requiring "the contractor to identify those supplies it did not manufacture..." supports our position that a subcontract "pass-on" is not warranted. In any event, fairness would dictate that subcontractors should not be included if they occupy the same exempt status accorded to a prime contractor.

5. The two sections contained the admonition, "nothing in this section requires the submission of cost or pricing data not otherwise required by law." The implementing FAR language is silent on this point; our redraft corrects this omission. We do detect what appears to be a conscious attempt to "link," or subordinate, sections 1245 and 501 to the Truth in Negotiations Act, as implemented in FAR. Such action is not justified; in fact, the last sentence in each section, quoted above, supports that conclusion.

We call to your attention the July 29th Congressional Record. In considering the 1986 Defense Authorization Bill, within Title IX, there is a section 914 entitled, "Regulations to control prices that may be paid for spare parts:" the material appears on page H6645. CBEMA submits that these latest Congressional expressions further support our position, i.e., that the correct focus of section 1245 (and its companion section 501) is spare parts. Moreover, there is nothing to suggest that this latest Congressional action is as expansive in its purpose and result as the FAR Council's Item II work product implementing sections 1245 and 501.

CBEMA recommends that the FAC 84-10 revisions under Item II, Integrity of Unit Prices, be immediately rescinded. As presently issued, the language is clearly overreaching, inconsistent with Congressional intent, and ambiguous for lack of definitions. CBEMA representatives wil be pleased to work with you, through an orderly rulemaking process, to properly implement the aforementioned sections 1245 and 501. To this end, we offer the enclosed redraft of the relevant FAR sections. This redraft represents a workable, administrative implementation of the statutory provisions and the problem Congress was seeking to redress.

Sincerely,

Vico E. Henriques

Vico E. Henriques
President

VEH:cls

Enclosures: 2

cc: Mr. Stuart J. Evans, Assistant Administrator for Procurement, NASA
Honorable James P. Wade, Jr., Assistant Secretary for Defense for Acquisition and Logistics
Honorable Terence C. Golden, Administrator, GSA
Mr. Robert P. Bedell, Acting Administrator, Office of Information and Regulatory Affairs, OMB
Mr. William E. Mathis, Acting Administrator, Office of Federal Procurement Policy, OMB

bcc: Mr. Alan R. Yuspeh, General Counsel, Senate Armed Services Committee
Mr. Alan L. Chvotkin, Counsel for the Minority, Senate Armed Services Committee
Mr. William B. Montalto, Procurement Policy Counsel, Senate Small Business Committee
Mr. John M. Duncan, Staff Director, Senate Governmental Affairs Committee
Mrs. Colleen Preston, Counsel, House Armed Services Committee
Mr. William M. Jones, General Counsel, House Government Operations Committee
Mr. Stephen M. Daniels, Minority Staff Director/Counsel, House Government Operations Committee
Honorable James C. Miller, Chairman, Federal Trade Commission

Digest of Relevant Legislative History

The review of the history leading to passage of the legislation cited in Items II and III is most instructive. It is particularly important to note the origin of the legislation, the setting in which it was introduced, and the remarks of the author at the time it was taken up for legislative action.

It should be observed at the outset, that the two provisions appearing within the 1985 Defense Authorization Act (P.L. 98-525) preceded their counterparts in the Small Business and Federal Procurement Competition Enhancement Act of 1984 (P.L. 98-577). Basically P.L. 98-577 "borrowed" these two provisions from the Defense Authorization Act passed eleven (11) days earlier In the same vein, when the Senate took up the 1985 Defense Authorization Act, it adopted in large measure the House's H.R. 5167 in substitution for S. 2723. In this context, compare the House-passed H.R. 5167, Section 812 (which proposed new code sections 10 USC 2320 and 2321) with the Senate version of H.R. 5167 with its Sections 192 and 199. The prime focus is therefore on the action by the originating body--the House of Representatives.

1. H.R. 5064 was introduced on March 7, 1984 by Rep. Nichols. Entitled the "Defense Spare Parts Procurement Reform Act," the bill was introduced after extensive "spare parts" hearings by the Investigations Subcommittee of the House Armed Services Committee. The Committee Report (98-690), dated April 18, 1984) in its "Background" and "Discussion" sections indicates that the focus was limited to correcting the perceived inflated and excessive prices for spare parts. Section 2 of the Report, Congressional Findings and Policy Direction, also reveals that the proposed legislation was directed at "...elimination of excessive pricing of replenishment parts..."

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3. The two aforementioned sections were the forerunners and the basis for the present enactments under consideration.

   a. As to the overhead provisions, proposed section 2321, it was evident that the author was not viewing the normal commercial channel as the nexus of the problem. Note that subsection (d) recited:

      "This section does not apply to a contract for the purchase of spare or replacement parts from a contractor who is a regular dealer in such parts...."

      In his comments, after introducing his amendment, Rep. Bedell stated:

      "...it requires that only overhead applicable to the part can be charged to the Government. This will eliminate the ways the contractor justified $435 for a $7 hammer." (Congressional Record, May 30, 1984, p. H4932)

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      "...it requires contractors to supply parts at their lowest commercial price or justify reasons for any higher charge." (Congresional Record supra)

4. Subsequent discussion of the Bedell amendment did not focus on this proposed language of sections 2320 and 2321. In particular, it did not suggest, or hint, that the provisions should be expanded to include other than spare or replacement parts having commercial application.

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reference to the previous passage in the House of the Bedell amendment (see Congressional Record, June 20, 1984 at page S7817). Again, there is nothing in the floor discussion that suggested an expansion beyond spare parts or the criteria, "lowest price available...to commercial buyers."

7. Section 1245 of P.L. 98-525 represented the Conference Committee result, after considering the House language (Section 812, with its proposed new code section 2321, "Fair distribution of overhead charges for spare parts") and the Senate's version Section 192, "New regulations for allocating overhead to parts to which the prime contractor has added little value." The Conference Report 98-1080 (dated September 26, 1984), on pages 326 and 327, clearly reflects the area of Congressional concern, i.e., acquisition of spare or replacement parts and common items from other than normal commercial manufacturing and distribution channels so that the purchase price bears no relationship to the intrinsic value of the item. Moreover, the focus was on, as the title suggests, acquisition of parts "to which the prime contractor has added little value." There is no statutory basis for imposing or "passing on" the requirement to lower-tier subcontractors, as the FAR Circular clause mandates.

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   The Senate amendment contained a similar provision (Sec. 199)." (emphasis added)

In conclusion, the expansive language and thrust of the FAR material is not supported by the voluminous legislative history, which indicates the specific problem area (commercial parts) and the specific "yardstick" (lowest price to commercial customers) that Congress was addressing.

ENCLOSURE II

15.812 Unit Price

15.812-1 Definitions and Application

(a) Throughout 15.812 and 52.215-26, wherever used, the following terms shall be defined as set forth below:

(1) "Item" or "item of supply" means any individual part, component, subassembly, or subsystem integral to a major system, and other property which may be replaced during the service life of the system, and includes spare parts and replenishment spare parts.

(2) "Commercial item" is an item regularly used for other than Government purposes and sold or traded to the general public in the normal course of business operations.

(3) "Manufacturer" and "regular dealer"--see 22.606-1 and 22.606-2 for definitive criteria.

(b) The provisions of 15.812-2 are not applicable when the item being procured is a commercial item and the offeror/prime contractor is the manufacturer, or a regular dealer, of the commercial item. In this context, the aforementioned provisions are also inapplicable if the agency places a contract under the General Services Administration's competitive multiple award schedule program.

15.812-2 General

(a) Although direct and indirect costs are generally allocated to contracts in accordance with the Cost Accounting Standards of Part 30 (when applicable) and the Contract Cost Principles and Procedures of Part 31, for the purpose of pricing all items of supplies, distribution of those costs within contracts shall be on a basis that ensures that unit prices are in proportion to the item's base cost (manufacturing or acquisition costs). Any method of distributing costs to line items that distorts the unit prices shall not be used. For example, distributing costs equally among line items is not acceptable except when there is little or no variation in base cost.

(b) When contracting by negotiation, without full and open competition, contracting officers shall require that offerors identify in their proposals those items of supply which they will not manufacture or to which they will not contribute significant value. Such information shall be used to determine whether the intrinsic value of an item has been distorted through application of overhead and whether such items shall be considered for breakout.

(c) Nothing in this section requires the submission of cost or pricing data not otherwise required by law, as implemented (see 15.804).

15.812-3 Contract Clause

When contracting without full and open competition, the contracting officer shall insert the clause at 52.215-26, Integrity of Unit Prices, in all solicitations and contracts, except:

(a) small purchases under Part 13; and

(b) to the extent any soliciation or contract involves--

(i) construction or architect-engineer services under Part 36;

(ii) utility services under Subpart 8.3; or

(iii) commercial items where the offeror/prime contractor is the manufacturer or regular dealer.

52.215-26 Integrity of Unit Prices

As prescribed in 15.812-3, insert the following clause:

Integrity of Unit Prices (June 1985)

(a) Any proposal submitted for the negotiations of prices for items of supplies shall distribute costs within contracts on a basis that ensures that unit prices are in proportion to the items' basecosts (e.g., manufacturing or acquisition costs). Any method of distributing costs to line items that distorts unit prices shall not be used. For example, distributing costs equally among line items is not acceptable except when there is little or no variation in base cost.

(b) The offeror/contractor shall also identify those items which it will not manufacture or to which it will not contribute significant value.

(End of clause)

CBEMA

August 9, 1985

General Services Administration
Attn: FAR Secretariat (VR)
Room 4041
18th and F Streets, N.W.
Washington, DC 20405

SUBJECT: Federal Acquisition Circular 84-10
REFERENCE: Federal Register Notices of July 3 and 10, 1985

Dear Sir:

This letter is submitted in response to the notice and request for comments that appeared in the July 3, 1985, Federal Register, Volume 50, pages 27560 through 27563, and corrected in 50 FR 28103 dated July 10, 1985. Although FAC 84-10 contains five items, this letter addresses Item III, Certification of Commercial Pricing alone. By separate letter CBEMA will comment on Item II, Integrity of Unit Prices. The substance of this letter and the enclosed redraft of FAR 15.813 and FAR 52.215-32 are consistent with and additive to the CBEMA and EIA joint letter dated August 2, 1985. In addition to furnishing the substantive comments on the text of Item III, we must strongly object to certain procedural criteria associated with release of the circular as follows:

a. It appears to be completely contrary to the intent of 41 U.S.C. 418b(d) to issue FAC 84-10 as a temporary regulation having immediate effect as a waiver to the requirements of 41 USC 418b subsections (a) and (b), three months after the date by which the regulation should have been issued pursuant to the Defense Authorization Act of 1985 and the Small Business and Federal Procurement Enhancement Act of 1984. This is clear since in this almost nine-month period since passage of the legislation no comments were sought from the many interested parties. Having reached this point, there could be no compelling reason not to go through the normal rulemaking process, since an additional thirty days would have been added for comments, so a final regulation would be issued without the ambiguities and the expansion of the scope of the statute which the temporary regulation contains.

b. There also has been a gross underestimate of the records which must be reviewed, the records which must be retained, the amount of information which may have to be furnished, and the time and cost for review and retention. Therefore the report furnished to the Office of Information and Regulatory Affairs (OIRA) pursuant to 44 USC 3504 contains gross errors which are misleading and distort the findings of the Director, OIRA, which are required by 44 USC 3504(h).

Computer and Business Equipment Manufacturers Association 311 First Street, N.W., Suite 500, Washington, D.C. 20001 (202) 737-8888

As back-up to our assertion that the estimate, submitted to OMB/OIRA, of the information and recordkeeping burden placed on industry is a gross underestimate, we submit the following points:

(1) The FAR Secretariat's submission of June 21, 1985, to OMB/OIRA estimates the time required to assemble and prepare a response to the certification/statement requirements as twenty minutes per line item of a solicitation. This estimate assumes 100% automation of contractors' records. We do not believe this assumption of 100% automation is factual. In addition, CBEMA member companies indicate that the 20-minute per line item estimate is only a small fraction of the staff and management time which would be required to either certify or to justify price differentials. Furthermore, the calculation appears to be based upon an assumption of only one line item per solicitation. This is clearly not realistic.

(2) The estimate referred to in (1) is based upon an estimate of 4,756 respondents per year. Converstions with Civilian Agency Acquisition Council and Defense Acquisition Regulatory Council staffs have not provided us with a factual basis for this number. Our check with GSA reveals that GSA alone has 12,431 schedule contracts (11,781 FSS and 650 OIRM).

(3) The FAR Secretariat's documentation shows the estimated number of recordkeepers per year as 300. The explanation we have received for this number is that 300 is the estimate of the number of audits the Government could conduct per year. The flaw in the logic of this calculation is quite obvious. The number of recordkeepers is not determined by the number of audits per year, but rather by the total accumulated number of active contracts having the recordkeeping/audit clause in them. Even if the 4,756 respondents number is accurate (which we doubt), the first-year number of recordkeepers would be closer to that number than 300. Additionally, the number per year after the first year will grow dramatically as the number of active contracts with the recordkeeping/audit clause grows cumulatively each year.

(4) One of CBEMA's member companies has done a ballpark estimate of the price to implement an automated system to meet the information and recordkeeping requirements of FAC 84-10. This estimate is a onetime start-up figure of $11.5 million and a $9.5 million annual recurring figure.

Legislative History

It is clear from a review of the legislative histories of P.L. 98-525 and P.L. 98-577 (which must be viewed together because of the closeness in time of debate and passage) that the issue Congress was addressing involved spare parts. Enclosure I is a digest of some of the relevant legislative history to illustrate that crucial point.

Moreover, the language of 41 USC 253e and 10 USC 2323 as enacted refers to "items," and 41 USC 403 (the codification of P.L. 98-577) defines the term "item" as "any individual part, component, subassembly, assembly, or subsystem integral to a major system, and other property which may be replaced during the service life of the system...." This is a much narrower definition than that of "supplies" set forth at FAR 2.100, some delimiting factors being that "items" are part of a large supply which is further defined as a major system and the items must be replaceable. The concept of replacement covers provisioning, spares and related items which are incidental to or part of one or more elements of a major system. Thus, it seems clear that the legislative interest manifested by the legislative history was continued in the substantive drafting of 41 USC 403.

Furthermore, the definition of "item" contained in 41 USC 403 is Government-wide and not limited to Civilian Agencies alone. Therefore it is a clear overreaching extension of the legislative intent when FAR defines "item" as quoted above to be applicable to Civilian Agencies alone and not to NASA and DOD. As the regulation is now written, 15.813-3(a) calls for certificates and/or statements for anything offered for sale to the public, unless otherwise exempted, in the case of NASA and DOD. In fact, a closer reading of the plain language of the statute consistent with legislative intent emphasizes that the sole specific thrust of the statute was in the spare parts arena. In that context "item" refers, in reality, to spare and replenishment parts. Spares normally are not competed. They are sole-source and follow-on to the winning sytem contractor. Therefore, unless there was full and open competition permitted for replenishment or replacement of commercial parts, subassemblies, components and subsystems that make up the elements of a total major system, a contractor could potentially be able to charge the Government whatever it wished.

Furthermore, since the item being provided is a commercial item (i.e., an item sold in substantial quantities to the general public) the contractor would not be required to furnish cost data or price data. Therefore, Congress provided that unless "full and open competition" was permitted for commercial "items" (i.e., items of supply which were replenishment or spare parts, components, subassemblies, etc., of the elements of a major system), a contractor would be required to certify that the prices for those replenishment or spare parts were no higher than the lowest price charged to others (i.e., the public) in the past 60 days for those "same" items. By "same" items they meant the same quality, the same quantity, the same delivery and the same terms and conditions. If the replenishment or spare commercial items being sold to the

Government were not the "same," no price certification would be required. If full and open competition between responsible bidders was permitted, no price certification would be required. Finally, if neither of these occurred but national security required it, no price certification would be required. All of this is simple enough and laudable in purpose.

The problem is that the regulation has gone beyond the statute and swept in other than replenishment and spare parts, etc., for major systems. It also has provided for a sweeping audit right not required by statute and an audit right which appears literally to have gone far beyond mere verification of the equally low price. Moreover, the regulation has overreached by giving the Government discretion to require a price certification and audit where the Congress plainly did not require it. Lastly, the regulation prescribes cumbersome, impracticable and unworkable mechanics because certain vital definitions are lacking which, if present, would perhaps make the accounting workable.

FAC 84-10; FAR 15-813, Commercial Pricing Certificates

In order to deal with the problems associated with the FAC 84-10 implementation of the two statutes in an orderly and logical manner, we have included in this section our comments and a paragraph by paragraph analysis of our major concerns about the temporary regulation. We thus point up by illustration major ambiguities, inconsistencies, and areas in which the regulation grossly overreaches the thrust of the statute. Considering the problems caused by ambiguities and inconsistencies in the regulation, we have enclosed hereto as Enclosure II a completely rewritten draft of FAR 15.813 and FAR 52.215-32, consistent with the statute and in keeping with our interest in seeing a clear, fair, and administratively feasible implementation of the statutory mandate.

1. FAR 15.813-1 Policy. The policy statement should comport with the statute by making clear that the commercial pricing approach contained in the policy statement applies where competitive procedures (i.e., full and open competition) have not been used, consistent with the statute.

2. FAR 15.813-2(a). To be internally consistent within the FAR and with the underlying statutes, this subparagraph should state that, except as provided in 15.813-3 the certification/statement described in FAR 52.215-32 will be submitted with any offer/proposal...."

3. FAR 15.813-2(a)(3) must be amended for consistency with FAR 6.102(d)(3) and exempt awards and orders placed under Schedule Contracts pursuant to GSA's competitive multiple award program.

4. FAR 15.813-2(c) must be deleted since by definition and expectation, fair and reasonable prices are obtained when full and open competitions are conducted by the Government. Congress recognized this result in the underlying statute which specifically makes the Certificate of Commercial Pricing approach inapplicable when competitive procedures (full and open competition) have been used. Furthermore, both Congress and the FAR recognized the fairness of pricing associated with commercial offerings some time ago (see FAR 15.804-3(c), and P.L. 87-653) neither of which have been modified as a result of the current concerns with spare parts pricing.

   FAR 15.813-2(c) causes an additional problem as written by literally overruling Congressional intent in an unrelated area. The language of this section places it in conflict with the House Appropriations Committee in its FY'80 Defense Authorization Report (House Report 96-450) which stated that all future ADP procurement evaluations and decisions should be made on the basis of lowest total overall cost. The Competition in Contracting Act also emphasizes the use of lowest overall costs for all negotiated procurements irrespective of product or agency.

5. FAR 15.813-3(a). This provision must be modified to exempt from any of the requirements of 52.215-32 the acquisition of items defined therein for all Executive Agencies, not just Civilian Agencies, in accordance with applicable statutes. There appears to be no reason or basis to overreach in the cases of NASA and DOD by requiring a commercial pricing certification/statement for items which are not integral to a major system. Furthermore, in order to eliminate confusion, the regulation must require the Contracting Officer to state in the RFP that certain designated "items" as shown are components, subassemblies, etc., integral to a named major system so that an Offeror/Contractor can know what any required certification/statement and the related records search and recordkeeping apply to.

6. FAR 15.813-3(b). The word "ordinarily" must be deleted from this subparagraph since it is ambiguous and therefore problematical. More importantly, it provides a regulatory basis to allow the Contracting Officer at his discretion to request a certification/statement under 15.813-3(b)(3) when none is required by the statute.

7. FAR 15.813-3(b)(3). In view of the administrative burdens to both contracting parties which result from a frequent disclosure of the basis for price differences and the reviews and discussions occasioned thereby, recognition of the concept of advance agreements seem particularly suited to such matters as terms and conditions differences. Since most contractors offering items to the public have

standard offering terms and conditions which differ substantially from the terms and conditions applicable to Government contracts, entering into an advance agreement based on those differences for the items offered to both would exempt all such contracts and reduce the administrative burden to both parties.

8. FAR 15.813-4(a). This procedure must be corrected to recognize, as prescribed by the statute, that a price certification or a statement may be applicable.

9. FAR 15.813-4(b) This subparagraph, if not changed, will cause substantial confusion and the possibility of multiple certifications with some sort of a rolling 60-day cycle. This is virtually impossible for contractors selling from multiple locations to administer. When an offer which is not exempt from the requirements of FAR 52.215-32 is submitted, a certification furnished at that time must be considered sufficient and no additional certifications will be required in order to preclude the administrative nightmare that would result. A single certification/statement is all that is required, consistent with the underlying statutory intent.

10. FAR 15.813-4(d). This subparagraph must be rewritten to comport to the language of both the statute and the clause. The phrase "commercial prices offered were defective...." is meaningless in the context of this regulation. We must assume that the regulation meant to detail when the Contracting Officer has reason to believe that the certification/statement were inaccurate (i.e., lower prices were charged to the public in the preceding 60 days), the Contracting Officer should review those sales records.

11. FAR 15.813-5. This provision must be changed to insert the clause only when the certification is required. When a certification is not required, there is nothing to remedy or audit.

12. FAR 52.215-32. This clause is replete with provisions going beyond the statutory requirement, ambiguities, undefined terms, confusing requirements and language which conflicts with FAR 15.813. Thus, rather than attempt to outline all the needed changes, we refer you to our questions noted in our July 26th letter to Mr. Lawrence J. Rizzi. For your convenience a copy is enclosed hereto as Enclosure III. The rewritten clause is included as part of our draft of the regulation enclosed hereto and affords reasonable and fair answers to the questions we have previously raised. The ambiguities are, therefore, also removed.

The overreaching expansion of the statutory requirements which have been added by the temporary regulation cause us a great deal of concern. For example, the addition of "governmental instrumentality" to the certification requirements is beyond the scope of the statute and may actually impact the Government's ability to obtain competitive prices. This is so because contractors may not be willing to bid on procurements for small quantities of items subject to these provisions, or will not bid their best prices, in order to preclude the setting of an "artificial" bar for subsequent larger procurements which might be anticipated to be awarded in the near term.

FAR 52.215-32 overreaches by requiring any audit at all and in the breadth of the audit which is envisioned. The statute does not require such an invasion of contractor's commercial information. The audit provision, itself, dealing as it does with "pricing" instead of sales information, is potentially an extension of the scope of the statute, depending on how it is to be interpreted, and is an ambiguous term which may be used to conduct an invasion by cost-based procurement policy into the commercial sales arena.

We previously indicated that the burden placed upon industry by FAC 84-10 was grossly underestimated. In that regard, any careful analysis of that burden must consider its long term real effects. In the absence of any companion mechanism to offset significant additional record maintenance and recurring costs, many of the firms actively competing for Government business today will inevitably have to reassess their ability to recover these real costs, which carries with such recovery a concomittant cost increase to the Government. If, on the other hand, these costs cannot be passed on to the Government, the appropriateness of continuing in the competition becomes a fair question for the owners of the business. Therefore, both the cost impact if accepted by the Government, and the increased costs to the business if not recognized, result in higher costs to the Government through the imposition of these requirements which cause higher prices to the Government, if recognized, or decreased competition, if not recognized. Neither of those results are beneficial to the Government in these times.

In view of the foregoing, and considering the severe impact which this regulation will have unless its many ambiguities, inconsistencies and conflicts with Congressional declaration and intent are corrected, we urge you to rescind this temporary regulation. We will be pleased to work with you thereafter in an orderly process of rulemaking as contemplated by the statutes, the intent of which has not been followed, to properly implement 41 USC 253e and 10 USC 2323. In furtherance of this objective, we offer you the enclosed redraft of the regulation to illustrate a workable, administratively feasible implementation of the statutory mandate. We will be pleased to discuss this with you at the very earliest.

Sincerely,

Vico E. Henriques
President

VEH:cls

Enclosures: 3

cc: Mr. Stuart J. Evans, Assistant Administrator for Procurement, NASA
Honorable James P. Wade, Jr., Assistant Secretary for Defense for Acquisition and Logistics
Honorable Terence C. Golden, Administrator, GSA
Mr. Robert P. Bedell, Acting Administrator, Office of Information and Regulatory Affairs, OMB
Mr. William E. Mathis, Acting Administrator, Office of Federal Procurement Policy, OMB
Mr. Alan R. Yespeh, General Counsel, Senate Armed Services Committee
Mr. Alan L. Chvotkin, Counsel for the Minority, Senate Armed Services Committee
Mr. William B. Montalto, Procurement Policy Counsel, Senate Small Business Committee
Mr. John M. Duncan, Staff Director, Senate Governmental Affairs Committee
Mrs. Colleen A. Preston, Counsel, House Armed Services Committee
Mr. William M. Jones, General Counsel, House Government Operations Committee
Mr. Stephen M. Daniels, Minority Staff Director/Counsel, House Government Operations Committee
Honorable James C. Miller, Chairman, Federal Trade Commission

Digest of Relevant Legislative History

The review of the history leading to passage of the legislation cited in Items II and III is most instructive. It is particularly important to note the origin of the legislation, the setting in which it was introduced, and the remarks of the author at the time it was taken up for legislative action.

It should be observed at the outset, that the two provisions appearing within the 1985 Defense Authorization Act (P.L. 98-525) preceded their counterparts in the Small Business and Federal Procurement Competition Enhancement Act of 1984 (P.L. 98-577). Basically P.L. 98-577 "borrowed" these two provisions from the Defense Authorization Act passed eleven (11) days earlier In the same vein, when the Senate took up the 1985 Defense Authorization Act, it adopted in large measure the House's H.R. 5167 in substitution for S. 2723. In this context, compare the House-passed H.R. 5167, Section 812 (which proposed new code sections 10 USC 2320 and 2321) with the Senate version of H.R. 5167 with its Sections 192 and 199. The prime focus is therefore on the action by the originating body--the House of Representatives.

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3. The two aforementioned sections were the forerunners and the basis for the present enactments under consideration.

   a. As to the overhead provisions, proposed section 2321, it was evident that the author was not viewing the normal commercial channel as the nexus of the problem. Note that subsection (d) recited:

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15.813 Commercial Pricing Certificates

15.813-1 Policy and Definitions

(a) Where competitive procedures are not used, the Government should not purchase items which are offered for sale to the public at a price that exceeds the lowest price at which such items are sold by the contractor to the public unless the price difference is justified by the seller or unless exempt under 15.813-3. In this regard, this policy implements 10 USC 2323 and 41 USC 253e.

(b) Throughout 15.813 and 52-215.32, wherever used, the following terms shall be defined as set forth below:

(1) "Contractor" shall mean the corporation, partnership, or sole proprietorship furnishing the offer and shall not include affiliates, subsidiaries, parent corporations, or joint ventures to which the contractor is a party.

(2) "Public" means domestic United States end-user buyers other than Government, or affiliates, subsidiaries, or the parent of the offeror.

(3) "Price charged" means the price for the item stated in a contract with the public accepted or executed within a sixty-day or such other time period as may be specified prior to the certification/statement. The time period will be counted backwards from a point thirty days prior to the beginning of the month in which the certification/statement is furnished.

(4) "Item, item of supply, or supplies" means any individual part, component, subassembly, assembly or subsystem of an element of a major system which is integral to a major system, and other property which may be replaced during the service life of a system, and includes spare parts and replenishment spare parts, but does not include packaging or labeling associated with shipment or identification of an item.

5.813-2 Applicability

(a) Except as provided in 15.813-3, a commercial pricing certificate/statement of justification is required to be submitted with any offer/proposal covering any item or items that are offered for sale to the public which is submitted in connection with any of the following:

(1) Contracts not awarded on the basis of full and open competition.

(2) Contract modifications for the acquisition of new or additional items that are integral to a major system, (other than those modifications which are based upon terms, conditions, and prices of the contractor's GSA Schedule Contract(s) issued, pursuant to GSA's Competitive Multiple Award Program), but not including contract modifications that are within the scope and under the terms of the contract such as contract modifications issued pursuant to the Changes clause, or funding and other administrative changes.

(3) Orders under the provisioning line item(s) of a contract or under a Basic Ordering Agreement or under a similar arrangement except for Awards of Schedule Contracts and orders placed under a Schedule Contract issued pursuant to GSA's Competitive Multiple Award Program.

(b) If the contract, modification, or order is awarded without a definitive price, such as a letter contract or an unpriced order, the commercial pricing certification/statement is not required prior to award but rather will be submitted with the offer or proposal furnished to definitize the price.

15.813-3 Exemptions from Commercial Pricing Certifications/Statement

(a) A certificate of Commercial Pricing/Statement is not required in connection with the acquisition of items unless the items being acquired are of the type defined in FAR 15.813-1(b)(4). Where the items being acquired are not exempt from the certification/statement in accordance with the requirements herein, the Contracting Officer must so state in the RFP and include a listing of those line items for which the certificate/statement may be required.

(b) The Contracting Officer shall not require a certificate of commercial pricing/statement when -

(1) The simplified small purchase procedures of Part 13 are being used; or

(2) An order is placed under an indefinite delivery type contract (a certificate/statement is required in connection with the award without full and open competition of an indefinite delivery type contract); or

(3) The Contracting Officer determines that obtaining the commercial pricing certificate/statement is not appropriate because of (i) national security considerations; or (ii) differences in quantities, quality, delivery, or other terms and conditions of the Government RFP or contractor's offer from the terms offered to the public. Examples of difference in terms and conditions include, but are not limited to, warranties, patent and copyright provisions, discounts for payments in advance of delivery, advertising discounts, discounts to dealers and other resellers, etc. Advance agreements covering exemptions from the

requirements of FAR 15-813 and the provisions of the clause at FAR 52-215.32 are encouraged when offerors/contractors present to the Corporate Administrative Contracting Officer copies of terms and conditions for its offerings to the public which differ from the provisions of FAR, or other relevant information pertaining to subparagraphs (i) or (ii) above. A copy of the advance agreement may be included in any offer/proposal submitted by the contractor and the contracting officer thereupon shall determine that the certificate/statement is not required; or

(4) The contracting officer determines that no items offered to the public are included in the offer/proposal, contract, modification, or order.

15.813-4 Procedures

(a) When commercial pricing certificates or statements are required in accordance with 15.813-2 above, the contracting officer shall require the contractor to submit the certificate/statement as set forth in the clause at 52.215-32, Certification of Commercial Pricing. The contracting officer should assess market conditions for the items expected to be covered by the certificate/statement to determine whether the standard 60-day time period specified in the certificate/statement is appropriate. If the frequency of price fluctuations or other circumstances persuade the contracting officer that a shorter or longer period is appropriate, the time period may be modified accordingly, in which case the contracting officer shall document in writing the basis/rationale for such modification and include the revised time period and statement supporting it in the RFP. In no event, however, shall the total length of the period established exceed 120 days.

(b) Unless the RFP is cancelled and reissued, the certificate/statement submitted by the offeror when required by 15-813.52 shall be the only submission of a certificate/statement for that procurement except under the circumstances described in subparagraph (c) below.

(c) If, before agreement on price, the contracting officer learns that the certificate/statement is inaccurate, incomplete, or misleading, the contracting officer shall immediately bring the matter to the attention of the offeror/contractor, request a new certificate/statement, and negotiate accordingly.

(d) If, after award, the contracting officer learns or suspects that the certificate/statement furnished by the contractor was inaccurate, incomplete, or misleading, the contracting officer shall request an audit under authority of paragraph (b) of the clause at 52.215-32 to examine the records of sales to the public during the 60-day period (or such longer or shorter time as may be stated in the RFP) preceding the date of the certificate/statement (counted in accordance with FAR 15.813-1(b)(3)) to determine whether in fact the certificate/statement furnished was inaccurate, incomplete, or misleading.

(e) Individual or class determinations made under 15.813-3(b)(3) or (b)(4) will be documented in the contract file.

(f) Possession of a contractor's Certificate of Commercial Pricing is not a substitute for examining and analyzing a contractor's proposal.

15.813-5 Contract Clause

The contracting officer shall insert the clause at 52.215-32, Certification of Commercial Pricing, in all solicitations and contracts unless exempted under 15.813-3 or under the exceptions to applicability stated in 15.813-2(a).

52.215-32 Certification of Commercial Pricing

As prescribed in 15.813-5, insert the following clause: The 60-day period may be changed by the contracting officer in accordance with 15-813.4(a):

Certification of Commercial Pricing (July 1985)

(a) The contractor/offeror shall execute and submit to the contracting officer the following certificate and/or written statement with any offer/proposal as required by section 15.813-2 of the Federal Acquisition Regulation (FAR).

Certificate of Commercial Pricing

(1) Unless justified by (2) below, by submission of this offer/proposal, the contractor/offeror certifies to the best of its knowledge, information, and belief that the prices offered hereunder for those items included in this offer/proposal that the contractor offers for sale to the public are no higher than the lowest price charged to the public during the 60-day period determined in accordance with FAR 15.813-1(b)(3).

(End of Certificate)

(2) All items for which prices offered thereunder are higher than the lowest price charged to the public during the 60-day period determined in accordance with FAR 15.813-1(b)(3) are identified below (including the amount(s) by which such offered prices are higher) and a written statement explaining the differences is enclosed.

Items	Price Differences

(b) The contracting officer or representatives of the contracting officer who are employees of the Government shall have the right to examine and audit all sales books, sales records, sales documents, and other sales data of the contractor directly pertinent to the prices charged to the public during the 60-day period determined in accordance with FAR 15.813-1(b)(3) preceding the date of the certification submitted hereunder was furnished for those items covered by this offer/proposal which are also offered to the public. The contractor shall make these sales books, sales records, sales documents and other sales data available for examination, for a one-year period after the date of the certification at the location or locations at which they are kept in the ordinary course of business.

(c) If any price, including profit or fee negotiated in connection with this contract, or any cost reimbursable under this contract has increased because the certification in paragraph (1) of the Certificate or the information provided as justification in paragraph (2) of the Certificate was inaccurate, incomplete, or misleading, the price or cost shall be reduced accordingly and the contract shall be modified to reflect the reduction.

ENCLOSURE III

CBEMA

July 26, 1985

Mr. Lawrence J. Rizzi
Director, Office of Federal Acquisition
and Regulatory Policy (VR)
General Services Administration
18th and F Streets, N.W.
Washington DC 20405

Dear Mr. Rizzi:

In his mailgram of July 23, 1985 to the FAR Secretariat, Vico E. Henriques, President of CBEMA, expressed a number of CBEMA's major concerns regarding FAC 84-10, and requested that it be immediately rescinded. As also indicated in our mailgram, CBEMA's detailed written comments regarding the many problems created by this circular will be furnished in accordance with the Federal Register notice.

The new FAC 84-10 which went into immediate effect on July 3, 1985, contains a substantial number of significant ambiguities relative to FAR 15.813 and FAR 52.215-32. CBEMA's prime request remains that FAC 84-10 be immediately rescinded and its subjects be pursued in the normal open rulemaking process; but because the circular is now in effect, CBEMA's member companies urgently need guidance or clarification of these major ambiguities so they can make individual determinations as to how they can conduct commercial product business with the governnment pending the rescision of FAC 84-10. Please furnish prompt responses to the following questions so that the Contracting Parties will know how to operate under this circular in the current environment:

1. The regulation calls for incorporation into the contract of the audit provision of FAR 52.215-32 in cases where neither a certification nor justification is required. Since the audit is to determine that the certification is accurate, complete, and not misleading, it does not appear that an audit provision applies since there is nothing to audit. Please clarify this internal inconsistency which makes 52.215-32 ambiguous.

2. No definition of "contractor" has been included. We assume, although it is not clear, that subsidiaries are not included in the definition.

3. "Any other customer" is not defined. We assume it means only domestic end user customers since it would be virtually impossible to certify as to foreign sales, considering exchange rate fluctuations and the impact of foreign laws and regulations. Furthermore, in the case of domestic remarketer customers, there are the unique efficiencies and special terms and conditions associated with sales to resellers which clearly make reporting of those transactions inappropriate.

4. Throughout the regulation, the concern is with prices or sales, however in

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subparagraph (b) of FAR 52.215-32 the word "pricing" appears for the first time. It is clear from all the material preceding this subparagraph that the intent is to be able to consider directly pertinent records of sales to the public for the sixty day period preceding the certification for the item(s) offered to the government. Please furnish a definition of "pricing" which is stated in terms of "directly pertinent records of sales to the public" in order to implement the requirement that authorizes the examination of records of sales for the sixty day period immediately preceding the date of the certification.

5. The records to be retained hereunder deal with transactions other than the government contract containing the FAR 52.215-32 clause. Therefore, a retention period equal to three years after final payment of that contract seems to have no relevance to the records involved. Contractors with substantial commercial sales activities out of multiple sales offices will be required to maintain this huge volume of sales records for many years beyond IRS or any other record retention requirements. It would appear that subparagraph (b) confuses the sales records with contract records which will increase the cost and space requirements for records retention beyond anything now contemplated. This should be clarified to limit the retention period for the directly pertinent records of sales to the public to three years after the date of the certification.

6. Both the current FAR and FAC 84-10 at FAR 15.812-(1)(b) recognize that GSA multiple award schedule contracts have been awarded under competitive procedures. Therefore, please clarify the ambiguity with regard to treatment under FAR 15.813 by adding an exemption to cover orders issued under GSA multiple award contracts.

7. The certification requires disclosure of all lower prices charged during the preceding 60 days, and thus records of such "charges" must be retained under the audit provision. There is no definition of "lower prices charged." Do you mean contracts entered into during the sixty day period, or charges made (i.e. invoices for purchase of such item(s)) during the sixty day period?

CBEMA would appreciate your prompt attention to this very important matter.

Sincerely,

Ted Heydinger

Ted A. Heydinger
Vice President

cc: The Honorable Terence C. Golden

CBEMA

September 30, 1985

General Services Administration
ATTN: FAR Secretariat (VRS)
Room 4041
18th & F Streets NW
Washington, DC 20405

Ref: FAR Case 85-39

The Computer and Business Equipment Manufacturers Association (CBEMA) is pleased to submit the attached comments on FAR Subpart 27.4, Rights in Data and Copyrights.

CBEMA is the trade association of producers of information processing, business and communications products, supplies and services. Our 38 member companies had combined sales of more than $135 billion in 1984. They employ more than 1.6 million people worldwide.

Our comments are arranged in the order the referenced paragraph appears in the text. We wish to highlight two concerns which apply to the entire Subpart.

- Definitions will be crucial to the orderly interpretation of the guidelines found in FAR 27.4. You have not attempted to define several terms that must be defined if the Congressional intent of P.L. 98-577, to "...not impair any right....of any contractor with respect to patents or copyrights or any other right in technical data....", is to be achieved. For example, you have not attempted to define "developed at private expense" and what is meant by a "substantial contribution" to an end item. You must do this, for these and other definitions, and do it in open discussion with industry to arrive at mutually acceptable definitions to use in negotiations.
- There is unnecessary duplication in the DFARS with respect to rights in technical data and computer software. The "single system of Government-wide procurement regulations" is clearly the FAR - not the agency supplements. CBEMA does not believe that FAR 27.4, as presently written, achieves the degree of uniformity intended by the Congress when it established the FAR System.

Again, our thanks for being invited to comment on this important Subpart of the FAR.

Very truly yours,

Vico E. Henriques
President

Enclosure: Comments on FAR 27.4

VEH:cls

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CBEMA

CBEMA COMMENTS ON FAR SUBPART 27.4

RIGHTS IN DATA AND COPYRIGHTS

Definitions found in 27.401 and elsewhere - Throughout the instructions and clauses, there are undefined terms which are key to the negotiation process. For example, the terms "developed at private expense," "published" (as in "published copyrighted computer software") and "minor modification" (as in "constitutes minor modifications to ..... limited rights data.") all need to be defined. CBEMA believes these terms should be defined in the FAR, not in the agency supplements to the FAR.

We have modified the definition of "developed at private expense" that was published for final comment in the DoD FAR Supplement Subpart 227.4 and related clauses in DFARS Part 252. CBEMA's definition broadens the kinds of data and computer software that would be covered by the definition, "developed at private expense," in order to afford a contractor a greater measure of protection for his investment. The definition reads as follows:

> "Developed at private expense", as used in this subpart, means that development was accomplished without direct Government payment and was not specified as a funded element of contract performance. The word "developed," as used in this phrase, means generated at private expense. When, in applying these criteria, an item, component, process or software package does not meet the test because the entire item, component, process, or software package cannot meet the definition, separate elements thereof which do meet the criteria will be considered to have been developed at private expense. In applying the foregoing criteria, when an item, component, process or computer software which has been developed at private expense is modified or revised to meet Government requirements specified in a contract, modification of the item, component, process or computer software shall not be considered to have been developed at private expense. However, the modification will not, of itself, entitle the Government to unlimited rights in the technical data and computer software that accompany the modified item, component, process or software.

Although the DFARS do not define "published," adoption by NASA and other Government agencies of the DoD definition of "unpublished" would be appropriate and helpful.

Acceptance by NASA and the civilian agencies of this definition would mean that software could be delivered with disclosure prohibitions -- and, accordingly, such practice for much of industry would recognize industry's security and control type provision in the typical computer software license agreement.

The NASA proposal to subject copyrighted computer software to full disclosure could also possibly be an argument to permit DoD to downgrade restricted rights software to unlimited rights. (See item "viii" on page 3 of the proposed DoD regulations.)

The term "minor modification" is also vague and does not appear in the operative clause at FAR 52.227-14(b)(1), where it is stated that the Government shall have unlimited rights in "data first produced in the performance of this contract." Patent and copyright laws have long recognized that derivative works are entitled to similiar protection as original works. Often, derivative works are more than mere minor modifications. Without this protection, industry will lose its incentive to create derivative works and to develop innovations to existing technology.

The use of two similiar terms, "data" and "technical data" is confusing. Using the single term "technical data" is preferable and more consistent with general industry usage.

The definition of "technical data" in 27.401 is distinctly different than that found in P.L. 98-577, amending Section 102 of the OFPP Act. Congress included the same definition in P.L. 98-525, to amend 10 USC 2310. The definition is intended to apply to all agencies.

The definition of "technical data" in the Acts includes computer software documentation; the definition in 27.401 does not. The definition found in the Acts excludes "computer software:" the definition of "computer software" in the FAR includes software documentation. Clarification is needed here.

27.402 - The policy statement is not balanced, nor does it comply with the statutory requirements. The "need" of the Government is to be balanced against the contractor's "legitimate proprietary interests." Section 301 of P.L. 98-577 amends the OFPP Act to require definitions of the legitimate proprietary interests of both and mandates that the rules shall not impair the rights of either party in technical data established by law.

This certainly includes trade secret laws and 18 USC 1905. The need for contractors to preserve their commercial markets for privately developed items, including privately developed improvements, should be clearly stated in the policy, with an injunction against destroying proprietary data rights for privately developed items, processes and components, when other measures, such as direct licensing, will satisfy the Government's minimum needs. Towards this end, we refer to NASA FAR Supplement 1827.472, Policy, which attempts to do this but lacks a specific prohibition against unnecessary buying of unlimited rights. The guidance would be most appropriate to subsections 27.402 and 27.406 as cautions against excessive zeal in acquiring data rights for competitive re-procurements.

27.404(c) - CBEMA does not see the need for two sets of criteria in order for data to qualify as limited rights data. The definition in Alternate I is adequate for all situations. To qualify, data need only be developed at private expense, embody a copyright or trade secret or be confidential or privileged.

27.404(d)(ii) - While the regulations provide for contractor assertions of conflict of interest if evaluation is made by certain non-Government evaluators (27.409(f)), they do not adequately address a situation where a non-Government evaluator compromises limited rights or restricted data. This issue has been a concern of CBEMA since evaluation by third parties was called for in P.L. 95-525.

27.404(e)(1)(i) The words, "or computers" should be deleted. Rights in technical data or computer software normally are assigned to a single computer item or entity. It should also be noted that the restrictions published in DFARS Subparts 227.4 and 252 do not use the updated language used here. CBEMA believes the wording should be identical Government-wide. Then the question becomes, should the restrictions have to be repeated in an agency supplement?

27.404(e)(1)(v) and a portion of the clause at 52.227-14, Alternate III - The words "for use" should be inserted after the word "reproduced". More importantly, CBEMA believes this portion of the clause does not adequately protect a contractor from unauthorized use or disclosure.

This portion of the clause is a departure from past civilian agency and DoD policy, as reflected in the old FPRs and DAR. It now gives a third party the right to use restricted software when no such right has been given by license. Disclosure and use of restricted software by a third party, including support contractors, should be obtained by means of a specific license granting such disclosure and use, and not as a standard exception within a restricted rights notice provision.

Language in the proposed DFARS is consistent with the old FPR/DAR policy. We refer you to the language at DFARS 252.227-7013(b)(3)(ii)(C) as a more positive control over the conditions under which third parties should have access to restricted software.

27.404(e)(2) - It is stated that, "Any additions to, or limitations on, the restricted rights set forth in the Restricted Rights Notice of subparagraph (g)(3) of the clause are to be expressly stated in the contract .... AND THE NOTICE MODIFIED ACCORDINGLY." (emphasis added) Is this intended to require that such additions or limitations be actually specified on the notice itself? If so, this is quite impractical and unnecessary. The Restricted Rights Notice, in subparagraph (d), states that, "Any other rights or limitations ..... are to be expressly stated in the contract." This is sufficient, without requiring such other rights or limitations to be detailed on the notice itself. At a minimum, the requirement should be modified to read "....... OR the notice modified accordingly." (emphasis added)

27.408 - In the second line, the words "substantial contributions" are used to distinguish who - the Government or the contractor - ought to hold the rights to any data pertaining to a deliverable item. "Substantial" is too ambiguous a term for such an important test.

27.409(d) - It should read "in accordance with 27.404(e)". In addition, see comment for 27.404(e)(2), above, which is also applicable to this provision.

52.227-14(a) - The definition of Restricted Computer Software should include at the end, "including minor modifications of such computer software." (See definition of Restricted Computer Software in 27.401.) Additionally, see comment for 27.401, above, which is also applicable to this provision.

52.227-14(b)(1)(i) - The parenthetical phrase "except to the extent such data constitute minor modifications to data that are limited rights data or restricted computer software" should be added at the end. (See 27.404(a)(1)).

52.227-14(b)(1)((iii) - The parenthetical phrase should be consistent with the parallel phrase in 27.404(a)(3) by substituting "as may be included with" for "for." More importantly, CBEMA objects to the authority of the Government under this clause to confiscate instructional and training manuals that are privately researched, developed and produced.

52.227-14(c)(2) - Since the scope of the copyright license granted to the Government for restricted computer software is limited to the rights set forth in subparagraph (g)(3) - Alternate III, the scope of the copyright license granted to the Government for limited rights data should be the same as the scope of the license granted for limited rights set forth in subparagraph (g)(2)-Alternate II. Clarification is needed here.

52.227-14(e)(i) - The procedures of this clause are to be triggered when data is delivered with the legends not authorized by this clause. The Government should be required to state in what respect such marking is improper. Collecting and submitting proof of data rights costs thousands of dollars not covered by the contract price. Therefore, unnecessary proof should be avoided.

52.227-14(f)(1) - The phrase "notice authorized by paragraph (g) below," should be deleted and in lieu thereof insert "restrictive markings." This change clarifies the fact that this subparagraph only applies where there is a complete omission or absence of any markings.

52.227-14(f)(2) - Delete this subparagraph and in lieu thereof insert the following:

> "If data authorized by the contract to be furnished with restrictions is received with restrictive markings not in the form prescribed by the contract, the data should be used in accordance with the restrictions provided for in the contract and the contractor shall be required by written notice to correct the markings to conform with those specified in the contract. If the contractor fails to correct the markings within 60 days after notice, Government personnel may correct the markings, and so notify the contractor."

This change seeks to fairly and reasonably define the rights and obligations of the Government and the contractor where the markings are "technically" incorrect (i.e. not in the precise form prescribed in the contract). Furthermore, all of the agencies should be able to agree on a single generic restrictive legend which would give appropriate notice and would not be the administrative burden that notice-making is at present. The proposed provision does not fully or adequately address all of the issues in this area.

52.227-14(g) - Insert the words, "the contractor," after the word, "data." Also, the so-called limited rights data in the last sentence of paragraph 'g' is a substantive part of a data base and should be treated as restricted rights data.

52.227-14(g)(2)-Alternate II - In the fifth line, "Contracting Officer" should be replaced with the word "Contractor."

In the limited rights notice, insert "written" after "without."

52.227-14 Alternate III - In the Restricted Rights Notice, item (b)(5) line 3, insert "and reproduction" after "disclosure."

52.227-14(g)(3)(ii)-Alternate III - In the just-released DFARS, the short-form restricted rights notice has different wording: DFARS uses "duplication" in place of "reproduction" and "as stated" in place of "set forth." CBEMA prefers the FAR wording, and recommends Government-wide uniformity be enforced.

52.227-14(g)(3)(iii) - Add another sentence to subparagraph (iii) of the clause, defining "unpublished." See CBEMA's comments, above, on the need for definitions of "published" and "unpublished."

52.227-19(b)(5) - Revise to read, in part, "....subject to the same restrictions under which the Government software is acquired."

52.227-19(c) - In line 3, change "(2)" to "(b)".

52.227-21(b) - It is impossible to certify to the completeness, accuracy and compliance of millions of data elements without the same qualifier found in the overhead certificate. After "hereby certifies," add the phrase "to the best of its knowledge and belief." The certificate also needs a date as to when the certificate applies.

CBEMA

October 9, 1985

Defense Acquisition Regulatory Council
Attn: Executive Secretary, DASD (P-DARS)
OUSDRE (M&RS)
The Pentagon, Room 3D139
Washington DC 20301-3062

Ref: DAR Case 84-187 (DFARS Technical Data)

The Computer and Business Equipment Manufacturers Association (CBEMA) is pleased to submit its comments on the DoD Federal Acquisition Regulation Supplement (DFARS) Subpart 227.4, Technical Data, and related clauses in Subpart 252.

CBEMA's 39 member companies represent producers of information processing, business and communications products, supplies and services. In 1984, our members had combined sales of more than $135 billion and employed more than 1.6 million people worldwide.

The revisions to the DFARS are being proposed to comply with P.L. 98-525, The Defense Procurement Reform Act of 1984 and P.L. 98-577, The Small Business and Federal Procurement Competition Enhancement Act of 1984. In CBEMA's judgment the revisions are seriously flawed and will need extensive rewrite to accurately reflect the intent of the two laws.

To begin, the entire Subpart must be reconciled with the FAR Subpart 27.4. In the CBEMA comments submitted to the FAR Council on September 30, we point out the absence of many definitions which are crucial to the orderly interpretation of the regulations. Without proper definitions of "developed at private expense," "mixed funding," "minor modifications ," and many more vague or undefined terms, it is not possible to use the parent regulation, much less the DoD Supplement, to reach equitable agreements on data right issues.

Second, Subpart 227.472, Policy, is clearly skewed in favor of poorly defined "needs" of the Government. The need for contractors to preserve their commercial markets for privately developed items, including privately developed improvements, should be clearly stated in the policy, with an injunction against destroying proprietary data rights for privately developed items, processes and components, when other measures, such as direct licensing, will satisfy the Government's minimum needs. The language in the laws regarding privately held rights in technical data and computer software are correctly stated in the regulation but are quickly followed by modifiers that convey a strong preference for acquisition of unlimited rights. For example, unlimited rights are not required as a precondition for obtaining a contract; however, an offerors willingness to provide "appropriate rights" will be evaluated. Similarly, the "necessity" for data takes precedence over the long-range

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commercial revenues foreseen by a contractor who wishes to develop commercial products with the same technology. In our enclosure we have outlined an approach which requires the Government to seek greater use of or access to data through a mandatory set of alternatives (licensing, leader/follower, etc.) before attempting the most difficult solution - total acquisition of unlimited rights.

Finally, CBEMA does not believe the DoD has met the intent of P.L. 98-525 Section 2320 (c) regarding the expiration of limited rights after a period of time specified in the contract. The law instructs the Secretary of Defense to "prescribe standards" to determine under what circumstances it shall be necessary to acquire unlimited rights after a period of time specified in the contract. Such written instructions should include, for example, a requirement that the contracting officer document the file as to why licensing and other options were not feasible before attempting to negotiate a time limit for limited rights.

In the attachment we have enumerated these and other serious concerns for your proposed change to the DFARS. In view of the magnitude of the issues, CBEMA suggests that you issue minimum, interim changes to the existing DFARS coverage on rights in technical data and computer software. Then, after a reasonable period of time to review comments and consult with industry, issue a fully revised subpart.

We wish to be kept informed of your progress in this important area and offer the assistance of our Association in reaching a mutually agreeable regulation.

Sincerely,

Vico E. Henriques
Vico E. Henriques
President

encl: Major CBEMA Points on DFARS 227.4

VEH:km

CBEMA

MAJOR CBEMA POINTS ON DFARS 227.4

- THE DFARS DISCOURAGES CONTRACTORS FROM OFFERING COMMERCIAL PRODUCTS BECAUSE OF THE THREAT OF COMPROMISE OR OUTRIGHT LOSS OF RIGHTS IN TECHNICAL DATA AND SOFTWARE.

  Discussion: The intent of Congress, as stated in Section 1202(4) of P.L. 98-525, is that "commercial parts be used whenever such use is technically acceptable and cost effective." The DFARS discourage this by applying the same test of commerciality for data purposes as is used for pricing purposes. The concept of "commercial" used in the statute is much broader and is based simply on "products or processes offered or to be offered for sale to the public." There should not be a difference in the definition of "commercial products" between the statute and the regulations that implement the statute.

- THE GOVERNMENT CRITERIA FOR ASSERTING A CLAIM FOR UNLIMITED RIGHTS SHOULD BE FUNDING AND PERFORMANCE; I.E., THE ITEM MUST BE DIRECTLY PAID FOR BY THE GOVERNMENT AND SPECIFICALLY REQUIRED AS AN ELEMENT OF PERFORMANCE IN THE CONTRACT.

  Discussion: The only test in P.L. 98-525 for determining rights in technical data or computer software is the source of the funds. Furthermore, the statute does not require private investment in R&D to be brought to the point of testing or reduced to practice. Here, as in our first point on "commercial products," we see a difference in definitions between a statute and a regulation. CBEMA has rewritten the draft DFARS definition of "developed at private expense" to include as part of the definition anything generated with the intent to develop for commercial purposes. Our suggested definition reads as follows:

  > "Developed at private expense", as used in this subpart, means that development was accomplished without direct Government payment and was not specified as a funded element of contract performance. The word "developed", as used in this phrase, means generated at private expense. When, in applying these criteria, an item, component, process or software package does not meet the test because the entire item, component, process, or software package cannot meet the definition, separate elements thereof which do meet the criteria will be considered to have been developed at private expense. In applying the foregoing criteria, when an item, component, process or computer software which has been developed at private expense is modified or revised to meet Government requirements specified in a contract, modification of the item, component, process or computer software shall not be considered to have been developed at private expense. However, the modification will not, of itself, entitle the Government to unlimited rights in the technical data and computer software that accompany the modified item, component, process or software.

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- THE REGULATIONS SUPPORT THE GOVERNMENT'S UNILATERAL CLAIM TO RIGHTS IN TECHNICAL DATA AND COMPUTER SOFTWARE FOR A VARIETY OF REASONS, MOST OF WHICH ARE IRRELEVANT. THE ONLY VALID TESTS TO DETERMINE WHO SHOULD HOLD RIGHTS ARE: (1) WHO FUNDED THE ITEM TO WHICH THE DATA RELATES, AND (2) WAS THE DEVELOPMENT OF THE ITEM OR DATA SPECIFIED AS AN ELEMENT OF PERFORMANCE IN A CONTRACT?

Discussion: In the previous DAR and in recent studies on data rights, the individual contract was the principle determinant as to who owns the rights to data and software. This important statement is missing for the new DFARS and should be added to subparagraph 227.472-1(b)(2) as follows:

> "Contract clauses and the schedule establish the form and type of technical data to be furnished; the categories into which such technical data fall, determine the rights to be obtained by the Government to use or publish such technical data."

Additionally, subparagraph 227.472-1(c)(1)(ii) erroneously implies that supporting software - regardless of origin - is to be delivered with unlimited rights. We recommend this subparagraph be changed to read:

> "(ii) Computer software required to be originated, developed or generated as a specified and funded element under a Government contract;"

- THE REGULATIONS DO NOT PROVIDE FOR AN ADEQUATE TEST OF MISSION NEED AS JUSTIFICATION FOR ACQUIRING UNLIMITED RIGHTS IN TECHNICAL DATA AND COMPUTER SOFTWARE. ALTERNATIVES TO UNLIMITED RIGHTS SUCH AS DIRECT LICENSING OR CO-PRODUCTION AGREEMENTS ARE NOT ADEQUATELY EXPLORED.

Discussion: Unlimited rights in technical data and computer software are neither a negotiation objective nor an absolute necessity. The real negotiating objective to be kept in focus is access to data, adequate enough to permit the agency to perform its mission.

Towards this end, two clarifications are needed in Subparagraph 227.473-2. First, the "various techniques for obtaining rights in technical data" should be prioritized, with acquisition of unlimited rights to privately held data being the least desirable alternative available to the contracting officer because of the significant expense to the Government and the impact on the commercial future of the items supported by the data.

Second, the statute instructs the Secretary of Defense to "prescribe standards" to determine under what circumstances it shall be necessary to acquire unlimited rights after a period of time specified in the contract. Such written instructions should include, for example, a requirement that the contracting officer document the file as to why licensing and other options were not feasible before attempting to negotiate a time limit for limited rights.

- NO GUIDELINES ARE OFFERED ON "MIXED FUNDING," WHICH IS THE CATEGORY OF DEVELOPMENT INTO WHICH MOST DISPUTES WILL FALL.

  Discussion: Data rights issues that go to courts and boards for resolution indicate that this is the most common area of dispute and the least likely to be agreed upon in the contract. P.L. 98-525 requires mixed funding to be "considered in prescribing such regulations." Yet, it is not defined or described in either the FAR or the DFARS, except insofar as the pre-notification procedures identify the claims of the contractor on data generated with mixed funding. This is an important area that needs clarification.

- PREDETERMINATION AND VERIFICATION PROCEDURES ARE BASED ON THE ASSUMPTIONS THAT THE GOVERNMENT'S INTEREST SHOULD PREVAIL AND THAT IT IS RIGHT FOR THE GOVERNMENT TO AGGRESSIVELY PURSUE THE ACQUISITION OF UNLIMITED RIGHTS IN DATA OR SOFTWARE.

  Discussion: The policy statement does not mention at all: 1) alternatives to complete acquisition of unlimited rights, such as the possibility of acquiring only form, fit and function data when this meets agency needs; 2) avoiding the acquisition of unnecessary data; or 3) adequately preserving the rights of the contractor. The DFARS statements in this regard should be compatible with the policy statement in the FAR.

- THE REGULATION OVERREACHES BY TYING PROPER DATA MARKING PROCEDURES TO WITHHOLDING OF PAYMENT.

  Discussion: Section 2321 of the statute provides guidance on validating and authorizes withholding of funds only for failure to deliver acceptable data. However, the regulation makes improper marking procedures a condition for holding that the data is nonconforming and therefore a basis for withholding of payment. Additionally, the clause at 52.227-7030 allows the contracting officer to withhold funds for anticipated failure to comply with contractual requirements pertaining to data.

- THE "LEGITIMATE PROPRIETARY INTERESTS" OF THE CONTRACTOR WILL NOT BE ADEQUATELY PROTECTED UNDER THE DIRECT LICENSING GUIDELINES SET FORTH IN THE REGULATIONS.

  Discussion: Section 2320 (a) of the statute requires that the legitimate proprietary interests of a contractor in technical and other data shall be protected. The proposed direct licensing clause at DFARS 52.227-7036 (e) requires the contracting officer to "direct the contractor, in writing, to license the technology in question to another source, including the extent of and the desired terms and conditions of any license." (Emphasis added.) For example, a requirement for unlimited rights to data for routine repair could easily require the loss of proprietary rights to design or manufacturing data. Similarly, the release of diagnostic software to a third-party contractor doing maintenance on a Government system, could result in the loss of restrictions on that software. This mandatory direction by the Government of terms and conditions clearly conflicts with the statutory requirement to protect the rights of the contractor.

- OTHER COMMENTS.

Government challenges to unmarked or improperly marked technical data or software: The DFARS as written strongly favors the Government. The Government should be required to state in what respect such marking is improper. Collecting and submitting proof of data rights costs thousands of dollars not covered in the contract price. Therefore, unnecessary proof should be avoided. Additionally, "clear and convincing evidence" required by 227.473-3 (c) should be changed to "written justification."

Certificate of technical data conformity: With reference to 227.474-3 (b) and the clause at 252.227-7037, it is impossible to certify to the completeness, accuracy and compliance of millions of data elements without the same qualifier found in the overhead certificate. After "hereby certifies," add the phrase "to the best of its knowledge and belief." The certificate also needs a date as to when the certificate applies.

Attachment 3

CBEMA

September 10, 1985

General Services Administration
Attention: FAR Secretariat (VR)
Room 4041
18th and F Streets, N.W.
Washington, D.C. 20405

SUBJECT: Federal Acquisition Circular 84-10
REFERENCE: Federal Register Notice of September 4, 1985

Dear Sir or Madame:

This letter and attached statement are submitted in response to the notice and request for comments that appeared in the September 4, 1985 Federal Register, Volume 50, page 35815. The attached written statement elaborates upon our oral statements made in the public meeting of September 10, 1985, which were, of necessity, limited by time constraints.

Given the considerable importance of the issues raised in connection with FAC 84-10, we welcome the opportunity to offer these comments. We also renew our offer to work with you in this matter in order to help resolve these issues in a manner which best serves the vital interests of all parties.

Sincerely,

Susan G. Stuebing
Director, Government
Procurement Programs

Attachment (1)

cc: Mr. Stuart J. Evans, Assistant Administrator for Procurement, NASA
Honorable James P. Wade, Jr., Assistant Secretary for Defense for Acquisition and Logistics
Honorable Terence C. Golden, Administrator, GSA
Mr. Robert P. Bedell, Acting Administrator, Office of Information and Regulatory Affairs, OMB
Mr. William E. Mathis, Acting Administrator, Office of Federal Procurement Policy, OMB
Mr. Alan R. Yuspeh, General Counsel, Senate Armed Serivces Committee
Mr. Alan L. Chvotkin, Counsel for the Minority, Senate Armed Services Committee

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Mr. William B. Montalto, Procurement Policy Counsel, Senate Small Business Committee
Mr. John M. Duncan, Staff Director, Senate Governmental Affairs Committee
Mrs. Colleen A. Preston, Counsel, House Armed Services Committee
Mr. William M. Jones, General Counsel, House Government Operations Committee
Mr. Stephen M. Daniels, Minority Staff Director/Counsel, House Government Operations Committee
Honorable James C. Miller, Chairman, Federal Trade Commission

September 10, 1985

Full Statement of the

Computer and Business Equipment Manufacturers Association

Before the

Civilian Agency Acquisition Council

and the

Defense Acquisition Regulatory Council

Reference: Federal Register Notice of
September 4, 1985

OVERVIEW

These comments are submitted in response to the notice and request for comments which appeared in the September 4, 1985, Federal Register, Volume 50, page 35815.

The Computer and Business Equipment Manufacturers Association (CBEMA) appreciates the opportunity afforded by this meeting and the Federal Register Notice of September 4, 1985 to address the important issues raised by Federal Acquisition Circular (FAC) 84-10.

CBEMA notes most favorably the very positive changes made in the FAC as reflected in the new draft which the Government released for review and comment on September 3, 1985. The FAC is demonstrably improved over the original version published on July 3, 1985.

Nonetheless, we see a number of very significant continuing problems in FAC 84-10, even as it has been redrafted in the September 4 version.

To save time and to permit the largest possible number of commentors to participate in this meeting, we have prepared a written statement which we are submitting to you at this time. In summary, however, the following points highlight our areas of concern:

- It is essential that the FAC be modified to reflect the stipulations of the law and the facts of the legislative history, by addressing its application clearly and only to the acquisition of commercial spare and replacement parts by other than competitive procedures. The statutory definition pertaining to items in major systems applies to all federal agencies and the FAC should reflect that fact.

- The actions by Congress in 1984, which FAC 84-10 seeks to implement, show no evidence of any intention to eliminate or reduce existing exemptions from submission of cost or pricing data in commercial product acquisitions. Accordingly, the FAC and its audit provisions should respect the long-standing reliance and acceptance of the Government on free market forces to establish fair and reasonable pricing and supply of off-the-shelf products. Any intimation of audit requirements for cost and pricing data on commercial products must be deleted. The audit provision should clearly call only for sales data needed to confirm the veracity of the certificate.

- The FAR clearly defines the terms "general public" and "commercial items" in a context which addresses all end-user customers other than the government. There is nothing in either the statutes or the legislative histories to suggest any Congressional intent to change these contracting principles. Accordingly, the FAC needs to be clearly modified so that relevant pricing is that pertaining only to end-user commercial customers, with no implication that the Federal Government itself sets, establishes or constitutes that marketplace. In addition, the FAC should clearly exempt all non-end-user prices as being without relevance to the Government or its treatment as a non-commercial end-user; such an exemption must logically treat as irrelevant all transactions with dealers, distributors, OEMs, remarketers, affiliates, subsidiaries, parent companies, company branches, and intra/inter-corporate transfers within the same business entity.
- The burdens imposed by the FAC, in their overall impact, should not exceed the burdens otherwise imposed by the statutes themselves. Any extension of the scope of the implementing regulations into areas not stipulated by the law must be discarded if the dislocations caused by the FAC are not to be most serious in their consequences to both industry and Government alike.

ISSUE #1

The original, published version of FAC 84-10 posed a major burden on industry in terms of both Management Information Systems (MIS) requirements and administration. The original paperwork estimates submitted to OMB/OIRA appeared to assume existence of standing MIS capabilities so comprehensive, in each commercial product company with which the Government does business, that execution of an individual certificate would take only twenty mintues. Moreover, the filing further appeared to assume that the required capabilities were so basic to these assumed systems that no additional administrative costs would be necessary, nor would there be any special system management or maintenance burdens separately identifiable to the requirements associated with FAC 84-10.

On examination of these apparent assumptions, it is our finding that the capabilities necessary to fulfill the requirements of FAC 84-10 simply do not exist on a standard basis in industry today. Therefore, it is entirely incorrect to assume that there are no separately identifiable costs or burdens associated with implementation of the FAC.

Even in the case of the revised draft of the FAC, there are still special information management capabilities which would have to be created to support its implementation. For example, the stipulation of including all Federal Agency contracts or sales to affiliates as being "commercial" sales, or, alternatively, classifying Government contracts or affiliate sales as being included in the meaning of the term "sale(s) to the public", is an entirely new concept in the field of federal procurement and its previous standard practices and far exceeds any previous requirements.

This concept also conflicts with fundamental Federal procurement policies. "Commerciality" has heretofore been a marketplace-oriented concept concerning business conducted with non-Federal and non-affiliated end-user customers; it was an objective of the Government to obtain the benefits of the products and prices forged in that marketplace. Indeed, the FAR clearly reflects a fundamental principle related to the United States' system where the Government is the recipient of the benefits of free commercial enterprise, as opposed to the Government setting, establishing or constituting that marketplace itself. As such, FAC 84-10 is without precedent and does damage both to the long-standing concepts of commerciality and the fairness and reasonableness of market-based prices.

The FAR is very specific with regard to these issues. Examples of relevant FAR principles include the following:

> 11.002 "...agencies shall acquire commercial products and use commercial distribution systems whenever these products or distribution systems adequately satisfy the government's needs..."
>
> 15.804-3(a) "...the contracting officer shall not require submission or certification of cost or pricing data when the contracting officer determines that prices are...based on established catalog or market prices of commercial items sold in substantial quantities to the general public..."
>
> 15.804-3(c)(3) "'Commercial items' are supplies or services regularly used for other than Government purposes and sold or traded to the general public in the course of normal business operations."
>
> 15.804-3(c)(5) "The 'general public' is a significant number of buyers other than the Government or affiliates of the offeror..."

FAC 84-10, as proposed, profoundly modifies the fundamental contracting principles detailed above. CBEMA strongly suggests that no modifications be made to these basic, accepted tenets of government procurement (including definition of fair and reasonable prices and exemptions from cost or pricing data disclosure) without a comprehensive review (with ample opportunity for public comment) of the economic impact to the Government and industry of such profound changes in the federal procurement system.

In going beyond the letter and intent of P.L. 98-525 and P.L. 98-577, the drafters of FAC 84-10 have significantly raised the level of regulatory impact and intrusion, including that of the administrative burdens addressed by the Paperwork Reduction Act. The burden created by FAC 84-10 is far greater than the paperwork burden associated with the actual requirements of the law.

The requirements of the FAC, and the assumptions of the filing at OMB/OIRA, do not take into consideration several key facts:

- Determination of the facts associated with any individual certificate could be very time-consuming, depending upon the degree and completeness of data automation. Firms that sell to the Government, like the Government itself, are not totally automated. Where automation exists, it is generally designed for internal purposes and not external requirements. If a corporation is organized with separate commercial and government divisions, and when the commercial entity is nationwide in scope, the problem of collecting and organizing the information required by FAC 84-10 is compounded. Hundreds of local sales offices must report through various regional sales branches who in turn, must report to a national sales headquarters. In order to execute a FAC 84-10 certification, an MIS with nationwide data communications capability would have to be established in order to collect the information from raw sales data to support certificates and justify situations where a given commercial end-user sale was lower than the price offered to the Government. If the final FAC includes provisions which apply to non-end-user sales, or Federal agency non-commercial/publi sales, or variable time period benchmarks, the requirements and costs associated with the necessary MIS capabilities are significantly increased.

- Assuming the likelihood of frequent certifications, given the breadth of coverage inherent in the FAC even as it has been redrafted, individual companies will have to dedicate multiple man-years of effort to the collection, monitoring, management, maintenance and certification of information in the degree, level of detail and manner required by the FAC. Even assuming a significant degree of existing automation, several member companies have projected a requirement for a dedicated 5-6 man-years of administrative effort annually; creation or modification of automated capabilities to support the necessary administrative man-years is at separate cost to each company; as noted in the CBEMA filing of August 9, 1985, one of our member companies has estimated the data systems cost at $11.5M for start-up, with another $9.5M in annual recurring expense.

- The potential impact of paperwork and administrative burden costs on the pricing of products themselves, and, in turn, the impact of those significant costs on the actual prices to be paid by the Government.

- The potential impact on trade of a lessening of competitive flexibility for domestic firms facing competition from unfettered foreign firms. This consideration manifests itself as a result of the FAC's over-reaching provisions requiring certification on all commercial products in Defense and NASA contracting, and in the implied requirement for cost and pricing data contained in the audit clause. These provisions provide for unprecedented Federal Government regulatory intrusion and oversight into competitive free market practices. This new regulatory reach would have an inevitably negative effect on the competitive flexibility of American firms, putting them at a distinct disadvantage vis a vis foreign competitors. It should be noted that the impact on trade was specifically not addressed in the submission to OMB.

The primary ways by which the administrative burden of FAC 84-10 could be readily reduced relate to the option of reformulating the FAC along the lines of the actual, more limited requirements of the law and existing provisions of the FAR. For example, the relevant sections of P.L. 98-525 and P.L. 98-577 have very clear and specific legislative histories which show the Congressional intent and objective as being regulation of the non-competitive acquisition of commercial spare and replacement parts. If FAC 84-10 were simply to be limited to implementation of the Congressional intent of the law the actual potential administrative burden would be significantly narrowed. Such modification/simplification would include the following changes:

- Limitation of applicablility to the acquisition of spare and replacement parts by other than competitive procedures; this restoration of the legislative intent would necessitate dropping the existing confusing references to "sealed bid acquisitions" (14.212) and "(in)adequate price competition" (15.813-2e) while adding a clear statement of inapplicability to procurements using full and open competition.

- Deletion of the first six words of the paragraph at 15.813-3(a). The limitation in the law in defining "items" and "items of supply" at 41 U.S.C. 403 as individual parts, components, subassemblies, assemblies or subsystems integral to a major system did not also contain any further limitation restricting the applicability of that definition to any lesser segment of the United States Government. Rather, the limitation to "civilian agencies, not including NASA" has been authored solely by the drafters of FAC 84-10. Given the substantial and consistent legislative history showing the Congressional intent as addressing the pricing of spare and replacement parts, and the total absence of any record showing the broader concept reflected in the FAC, there is no compelling basis for expansion of the certification requirement beyond the stipulations of the law. Indeed, this broadening very significantly impacts the business of government contracting, radically changing the government's reliance on the free marketplace for the private development and competitive supply of standard, off-the-shelf products.

- Reassertion of existing, accepted price benchmarks; the proposed

60-day, more or less, benchmark places new and significantly burdensome requirements on company data systems, and, moreover, is a requirement not stipulated anywhere in the law or legislative history. FAC 84-10 could be modified to adopt the following existing language from Standard Form 1412 - Claim for Exemption from Submission of Cost and Pricing Data (Instruction for Item 8): "This period should include the most recent regular monthly, quarterly, or other period for which sales data are reasonably available..."

- The broad audit rights which include "all books, data and documents" represent an expensive record-keeping burden which would be significantly reduced by clear limitation of the audit to pertinent sales data.
- Affirmation that records retention is for a specified period following certification, not following final contract payment; a twelve-month retention period for items which only must be retained due to FAC 84-10 would be a more manageable, cost-effective and reasonable requirement.

We further recommend the following specific modifications and clarifications:

- Clarification of the general applicability of the clause by insertion of the following paragraph at 15.813-3(b) as a new Subsection (5):

  "The Government is using competitive procedures and there is a reasonable expectation that adequate price competition will exist. If, subsequent to the issuance of the solicitation, it is determined that adequate price competition does not exist the Contracting Officer shall notify the offeror/contractor that a commercial pricing certificate is required in accordance with 15.813-2(e) and 15.813-4."

- Correction to 15.813-2(e), adding "not" in the second sentence to read:

  "To invoke this authority the Contracting Officer shall notify the contractor that a certificate is required under the terms of the clause at 52.215-32 if it was not included in the solicitation." (Emphasis added.)

- Clarification of 15.813-4, deleting the second sentence, "It should be noted...at the appropriate time", and adding the following:

  "Specific notice that a certificate is required shall be given by the Contracting Officer to the contractor. Notice shall be by inclusion of the clause in solicitations, modification or other documents as provided herein."

- Clarification of 15.813-5 by insertion of these words at the beginning of the paragraph: "In accordance with 15.813-2..."

- Clarification and simplification of 52.215-32(a) by modifying the language to read as follows:

  "...with any other end-user customer located in the United States, excluding a) any federal agency b) sales to subsidiaries, affiliates, parent companies and branches of the same business entity and c) sales to original equipment manufacturers, dealers, distributors and remarketers, during the most recent regular monthly, quarterly, or other period for which sales data are reasonably available before the date of this offer/proposal." (Changes underlined.)

- Clarification of 52.215-32(b) with the following modifications:

  "...examine and audit all directly relevant records, books, data and documents pertaining to sales, consistent with FAR 15.804, to verify the veracity of any certificate executed..."

ISSUE #2

CBEMA has no specific comments on Issue 2, but presumes that the comments on the other issues impact small businesses also.

ISSUE #3

The issue of types of sales to be considered in the definition of "the public" is well described in the comments already offered above on Issue #1, regarding federal agencies and sales to affiliated companies (i.e., subsidiaries, affiliates, parent companies, and branches of the same business entity). It has been clearly demonstrated that the exclusion of these two categories is consistent with specific FAR definitions, FAR exemptions for cost and pricing disclosure and the underlying procurement policies. In addition, their exclusion is also required by applying the ordinary meaning of the words.

Transactions with original equipment manufacturers, dealers, distributors and remarketers should also be excluded from the definition of "sales to the public". Commercial suppliers typically design, manufacture, distribute, sell and administer these products to the most competitive marketplace imaginable, the general public. These broad areas include a large number of individual functions and operations. The costs of these functions and operations are borne directly by the supplier when selling directly to end-user customers, such as the Federal Government.

The value to the supplier of an original equipment manufacturer, a dealer, distributor or remarketer is that such entities, in return for a discounted price specifically agree to assume the responsibility of and the expense for some combination of the functions and operations which the supplier would otherwise have to provide in order to get its products to the end-user. In other words, these entities are part of a supplier's distribution chain to get its product to "the public" or any other end-user. Even the antitrust and pricing laws distinguish between the various levels of the distribution chain and the ultimate users of goods and services. It would therefore be incongruous for these entities to be included in any manner in the definition of "sales to the public".

ISSUE #4

Again, this issue has been addressed in the comments offered on Issue #1.

Existing language such as that contained in Standard Form 1412 would simplify this issue. Requiring subjective judgements on appropriate market-sensitive time periods for different types of products would invite differing sets of guidelines, agency by agency, with widely inconsistent regulatory interpretation of relative products, technology, advancements, market fluctuations and other possible factors. This would represent yet another layer of new federal oversight with its binding interpretation of what does or does not constitute market factors legitimate for consideration in setting the time benchmarks. Through the proliferation of differing benchmarks, contractors could be subsumed by the confusion and variables of the burdens of such a situation.

Alternately, if individual agencies do not seek to establish implementing guidelines, the Government's internal burden then falls entirely upon the individual contracting officer to either conduct extensive continuing market research to determine appropriate, differing time benchmarks, or, in the absence of the ongoing time commitment needed to conduct such research, the contracting officer would have little alternative but to select time benchmarks which represent best subjective judgements, or even best guesses. This type of confusion, inconsistency, and burden on both the Government and industry, would be significantly mitigated by adoption of an existing practice as suggested in the reference to Standard Form 1412.

In seeking to come up with entirely new regulations, the Government has exacerbated the problem otherwise contained in FAC 84-10 as written, thereby increasing the paperwork and administrative burdens, and associated costs, for all parties, while unnecessarily complicating and damaging the acquisition process itself.

ISSUE #5

We have addressed this issue somewhat in our comments on Issue #1. In addition, we note that the original difficulty with the interim rule published in July went primarily to the retention of data for three (3) years past final contract payment, with no hint of any possible limitation to pertinent sales records. The problem as far as the question of sales records has been considerably mitigated by the changes reflected in the revised, draft FAC. The principal difference between the data required for FAC 84-10 and that required for the IRS and other instrumentalities goes to the ability to readily manipulate the data within automated systems in order to produce information useable by Government auditors for the specific purposes of Government contracting requirements. As such, the differences can be defined in the context of the management, formulation, organization and selection of pertinent information. Assuming the change in the retention period as proposed in the new draft of the FAC, it is in these other specialized areas that the requirements of the FAC diverge from the requirements of other agencies such as the IRS.

* * * * * * * * * * *

In conclusion, we wish to note two additional points which are relevant to your deliberations with regard to this important matter:

- We note with concern the absence of any reference to Item II, Integrity of Unit Prices, in either the September 4 Federal Register Notice or the new draft FAC discussed therein. We remain most concerned that Item II of the FAC must specifically correct any intimation that commercial prices of catalog products are in some way subject to cost and pricing analysis or disaggregation. Catalog prices of commercial items constitute a type of base cost which should not be reduced to some other incremental cost basis for Government contract purposes. All of the rationale which applies to the inviolability of the Government's reliance on free market forces for the development, pricing and supply of standard products, applies equally to the treatment of commercial products in Item II. We strongly urge the Government to modify Item II to clearly reflect these principles.

- Finally, we also note the unusual manner in which the FAC has been proposed and promulgated, going back to the initial publication of July 3, 1985. The process observed in the instance of FAC 84-10 has undeniably contributed to the difficulties, dislocations and confusion which still persist with regard to this rule. It is essential not only that the FAC be further modified, but also that the norms of open rulemaking be observed in future proceedings.

Attachment 4

NOTES FOR CBEMA ORAL STATEMENT
FOR SEPTEMBER 10, 1985 PUBLIC MEETING

OVERVIEW

- THE GOVERNMENT HAS MADE SOME VERY POSITIVE CHANGES IN THE 9/4/85 DRAFT FINAL REG.

- HOWEVER, CBEMA STILL HAS SOME BASIC MAJOR PROBLEMS WITH THE SCOPE AND REGULATORY OVERREACH OF THE DRAFT FINAL, WE SUGGEST THAT:
  - SHOULD BE CONSISTENT WITH THE LEGISLATIVE HISTORY --- PROCUREMENT OF SPARE & REPLACEMENT PARTS BY OTHER THAN COMPETITIVE PROCEDURES.
  - PRICE COMPARISON SHOULD BE TO THE LOWEST PRICE AT WHICH ITEM IS SOLD TO COMMERCIAL (NOTE: NOT FEDERAL) CUSTOMERS.

(NOTE: THESE TWO POINTS WERE RE-EMPHASIZED IN SEN. CARL LEVIN'S LETTER OF AUGUST 20TH TO DR. WADE, MR. GOLDEN AND MR. EVANS.)

  - EXPECTATION OF GOVERNMENT RECEIVING LOWEST PRICE SHOULD NOT EXIST WHERE CONDITIONS OF SALE AND USE ARE NOT THE SAME. THUS SHOULD BE END-USER CUSTOMERS AND SHOULD EXCLUDE:
    - ORIGINAL EQUIPMENT MANUFACTURERS, DEALERS, AND REMARKETERS
    - SALES TO SUBSIDIARIES, AFFILIATES, PARENT COMPANIES AND BRANCHES OF THE SAME BUSINESS ENTITY
  - SHOULD NOT ATTEMPT TO ALTER THE FREE FUNCTIONING OF THE COMMERCIAL PRODUCT MARKET OR OVERTURN LONG ESTABLISHED EXEMPTIONS FROM SUBMISSION OF COST AND PRICING DATA
  - THE COVERAGE SHOULD BE LIMITED AS PROVIDED IN THE STATUTE TO "CONTRACT ENTERED INTO USING OTHER THAN COMPETITIVE PROCEDURES"

- IN THIS REGARD WE BELIEVE THAT THE STANDARD APPROACH TO APPLICATION SHOULD BE THAT:
  - A. THE CLAUSE SHALL NOT BE INCLUDED IN SOLICITATIONS WHEN THE C.O. CONTEMPLATES THAT HE WILL RECEIVE TWO OR MORE RESPONSIVE BIDS.
  - B. IF THAT SITUATION DOES NOT ACTUALLY EXIST AFTER RESPONSES ARE RECEIVED, THEN THE C.O. BY SPECIFIC NOTICE SHOULD INFORM THE CONTRACTOR THAT A CERTIFICATE WILL BE REQUIRED, IF NOT EXEMPTED FOR OTHER REASONS.
- OUR WRITTEN STATEMENT CONTAINS SPECIFIC REGULATION LANGUAGE RECOMMENDATIONS TO ACCOMPLISH THIS.
- ALSO WE BELIEVE A "TYPO" EXISTS IN 15.813-2(e) OF THE DRAFT FINAL IN LINE 6. WE SUGGEST THAT THE WORD "NOT" WAS LEFT OUT, AND IT SHOULD READ: "IF IT WAS NOT INCLUDED IN THE SOLICITATION."

ITEM II - INTEGRITY OF UNIT PRICES

° WE NOTE WITH CONCERN THAT NEITHER THE DRAFT FINAL NOR THE 9/4/85 FED. REG. NOTICE ADDRESSES ITEM II - INTEGRITY OF UNIT PRICES.

° AS NOTED IN OUR SUBMISSION OF AUGUST 9TH ON ITEM II, WE CONTEND THAT:

1. THE LEGISLATIVE HISTORY ONLY SUPPORTS APPLICATION TO PROCUREMENT OF SPARE AND REPLACEMENT PARTS THROUGH OTHER THAN COMPETITIVE PROCEDURES.
2. THE CONGRESS IN ITS RECORD ON THE FY '86 DEFENSE AUTHORIZATION BILL HAS AGAIN INDICATED THAT THE FOCUS OF SECTION 1245, AND ITS COMPANION 501, IS SPARE PARTS.
3. THE LEGISLATIVE HISTORY CONTAINS NO SUPPORT FOR THE APPLICATION OF THE INFORMATION RQMTS OF 15.812-1(b) TO THE SALE OF COMMERCIAL PRODUCTS OR PARTS BY THE MANUFACTURER OR REGULAR DEALER THRU ESTABLISHED COMMERCIAL (CHANNELS) --- WE HOPE YOU HAVE ACCEPTED OUR RECOMMENDATION TO EXEMPT SUCH SALES

- STILL VERY DISTURBED BY LACK OF COOPERATIVE DUE PROCESS IN RULEMAKING.
  - CBEMA & EIA PROVIDED 24 HOUR TURN AROUND AFTER AUGUST 1ST MEETING.
  - LATE TUESDAY AFTERNOON AVAILABILITY OF FINAL DRAFT, FED REG NOTICE NEXT DAY ON PUBLIC MEETING AND 5 ISSUES, PUBLIC MEETING FOLLOWING TUES. WITH LITTLE INFO ON FORMAT IS NOT ADEQUATE FOR COMPANIES AND ASSOCIATIONS TO REACT.

ISSUE #1

- BASIC FLAW IN FAR SECRETARIAT'S PAPERWORK REDUCTION ACT SUBMISSION IS ASSUMPTION THAT 100% AUTOMATION OF CONTRACTORS' RECORDS CURRENTLY EXISTS --- THIS IS NOT TRUE.
  - IN FACT, ONE CBEMA COMPANY HAS ESTIMATED THE PRICE OF SUCH AN AUTOMATED SYSTEM AS:
    - $11.5M ONE TIME PRICE
    - $9.5M ANNUALLY RECURRING CHARGES

- ESTIMATING THAT BURDEN MUST CONSIDER THAT THE IMPACT WILL VARY FROM COMPANY TO COMPANY WITH MAXIMUM IMPACT UPON COMPANIES SELLING THROUGH MANY GEOGRAPHICALLY DISPERSED SALES OFFICES WITH LOCAL PRICING FLEXIBILITY.

- WE SUBMITTED A NUMBER OF SPECIFIC COMMENTS ON FLAWS IN THE ORIGINAL ESTIMATE IN OUR 8/9/85 SUBMISSION. MOST OF THOSE COMMENTS ARE STILL APPLICABLE TO THE DRAFT FINAL REG.

- AN ADDITIONAL EXAMPLE OF THE INACCURACY OF THE ESTIMATE IS THAT WHERE THE GOVERNMENT ESTIMATED 20 MINUTES TO PREPARE AND SUBMIT A RESPONSE, ONE OF OUR COMPANIES HAS ESTIMATED A BURDEN OF 4 MANAGEMENT/SENIOR STAFF PEOPLE FOR 4 DAYS JUST TO GET APPROVAL OF A CERTIFICATION/JUSTIFICATION AFTER IT'S PREPARATION.

- I DARE SAY A NUMBER OF CBEMA COMPANIES HAVE ALREADY FAR EXCEEDED YOUR ESTIMATE OF THE ANNUAL BURDEN PER RESPONDENT IN JUST ANALYZING AND REACTING TO THE FAC AND DRAFT FINAL.

ISSUE #2

CBEMA CANNOT COMMENT IN SPECIFIC DETAIL ON THE IMPACT OF THE FAC OR OF THE DRAFT FINAL ON SMALL ENTITIES AS OUR MEMBER COMPANIES ARE NOT SMALL BUSINESSES. HOWEVER, BASED UPON OUR ASSESSMENT OF THE IMPACT UPON LARGE AND MEDIUM SIZED BUSINESSES, WE JUDGE THAT THERE WILL BE EVEN MORE SIGNIFICANT IMPACT UPON SMALL BUSINESSES POSSESSING MUCH MORE LIMITED RESOURCES. THIS WOULD ESPECIALLY BE THE CASE IF THE APPLICABILITY IN DOD AND NASA IS TO THE PROCUREMENT OF ALL ITEMS AS PROPOSED BY THE FAC & DRAFT FINAL AS OPPOSED TO THE STATUTORY LIMITATION TO MAJOR SYSTEMS WHICH THE REGULATORY IMPLEMENTATION LIMITS TO CIVILIAN AGENCIES OTHER THAN NASA. SMALL BUSINESSES WOULD BE MUCH MORE LIKELY TO BE PRIME CONTRACTORS FOR MAJOR SYSTEMS.

ISSUE #3

- SALES "TO THE PUBLIC" SHOULD BE CONSISTENT WITH THE STATUTORY LANGUAGE AND ALREADY EXISTING FAR PROVISIONS:
  - STATUTES PROVIDE FOR LOWEST COMMERCIAL PRICE AND EXCLUDED SITUATIONS WHERE DIFFERENCES EXIST IN QUANTITIES, QUALITY, DELIVERY, OR OTHER TERMS AND CONDITIONS.
  - IN OUR INDUSTRY, THE GOVERNMENT BUYS AS AN END-USER CUSTOMER; CLEARLY THE CONDITIONS OF SUCH SALES ARE INHERENTLY DIFFERENT THAN SALES TO:
    - ORIGINAL EQUIPMENT MANUFACTURERS, DEALERS AND REMARKETERS.
    - SUBSIDIARIES, AFFILIATES, PARENT COMPANIES, AND BRANCHES OF THE SAME BUSINESS ENTITY.

(NOTE:

- THE LANGUAGE OF THE DRAFT FINAL DOES NOT CLEARLY COVER THE SITUATION EXISTING IN LARGE COMPANIES WHERE SUBSIDIARIES ARE SEPARATE COMPANIES.
- IN THIS REGARD WE FAIL TO UNDERSTAND WHAT IS MEANT BY THE DRAFT FINAL PHASE IN 15.813.4(b) "PRICES ... WERE NOT THE RESULT OF ARMS LENGTH NEGOTIATIONS")
  - THUS, THESE CATEGORIES OF SALES SHOULD BE EXCLUDED FROM THE CERTIFICATION/JUSTICATION REQUIREMENT.
  - THE DRAFT FINAL'S CERTIFICATE PROVISION "INCLUDING ANY FEDERAL AGENCY" IS INCONSISTENT WITH:
    - THE STATUTORY PROVISION OF LOWEST COMMERCIAL PRICE
    - FAR PROVISION IN: 15.804-3(c)(3) THAT "COMMERCIAL ITEMS ARE SUPPLIES OR SERVICES REGULARLY USED FOR OTHER THAN GOVERNMENT PURPOSES AND SOLD OR TRADED TO THE GENERAL PUBLIC IN THE COURSE OF NORMAL BUSINESS OPERATIONS." AND
    - 15.804-3(c)(5) "THE 'GENERAL PUBLIC' IS A SIGNIFICANT NUMBER OR BUYERS OTHER THAN THE GOVERNMENT OR AFFILIATES OF THE OFFEROR ..."

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ISSUE #4

- THE PROVISION ALLOWING THE C.O. TO VARY THE LENGTH OF TIME MIGHT POSSIBLY NOT PLACE SIGNIFICANT ADDITIONAL BURDEN UPON COMPANIES IF THE ASSUMPTION THAT 100% AUTOMATION OR CONTRACTORS' RECORDS CURRENTLY EXISTS WERE ACTUALLY TRUE.

- AS IT IS, CONTRACTORS WOULD BE REQUIRED TO DEVOTE SIGNIFICANTLY INCREASED PERSONNEL RESOURCES IN ORDER TO TRACK, RETRIEVE AND ANALYZE SALES RECORDS OVER PERIODS OF TIME WHICH MIGHT VARY FOR EACH AND EVERY PROCUREMENT FOR WHICH THEY WERE REQUIRED TO CERTIFY.

- WE RECOMMEND THAT THE BURDEN ON INDUSTRY COULD BE MINIMIZED BY ADOPTING THE APPROACH CURRENTLY USED IN THE EXISTING STANDARD FORM 1412 - CLAIM FOR EXEMPTION FROM SUBMISSION OF COST AND PRICING DATA (INSTRUCTIONS FOR ITEM 8):
  - "THIS PERIOD SHOULD INCLUDE THE MOST RECENT REGULAR MONTHLY, QUARTERLY, OR OTHER PERIOD FOR WHICH SALES DATA ARE REASONABLY AVAILABLE."

ISSUE #5

- THE MOST SIGNIFICANT PORTION OF THE BURDEN PLACED ON INDUSTRY BY THE INTERIM RULE WAS DUE TO THE PROVISIONS:
  - RECORDS HAD TO BE MAINTAINED FOR THREE YEARS AFTER FINAL PAYMENT UNDER THE CONTRACT; AND
  - ALL BOOKS, RECORDS, DOCUMENTS AND OTHER DATA OF THE CONTRACTOR RELATED TO THE PRICING OF THE COMMERCIAL ITEMS HAD TO BE KEPT.

- THE PROPOSED DRAFT FINAL SIGNIFICANTLY REDUCES THIS EXPOSURE IF THE TIME PERIOD IS LIMITED TO THREE YEARS FROM THE DATE OF CERTIFICATION AND IF THE BULK OF THE REQUIREMENT IS FOR SALES RECORDS. SUCH THREE YEAR RECORD KEEPING OF SALES RECORDS IS CONSISTENT WITH IRS RECORD KEEPING REQUIREMENTS. HOWEVER, OUR ASSESSMENT IS THAT THE DRAFT FINAL WOULD REQUIRE ABILITIES TO RETRIEVE AND ANALYZE THOSE RECORDS IN A MANNER SUBSTANTIALLY BEYOND IRS REQUIREMENTS.

Attachment 5

CBEMA

September 16, 1985

Mr. Lawrence J. Rizzi
Director, Office of Federal
Acquisition and Regulatory Policy
General Services Administration
18th and F Streets NW
Washington DC 20405

Mr. Michael D. Stafford
Acting Director, Defense Acquisition
Regulatory Council
Room B-105
1211 South Fern Street
Arlington VA 22202

Dear Mr. Rizzi and Mr. Stafford:

The Computer and Business Equipment Manufacturers Association (CBEMA) welcomes the opportunity to expand upon our comments in connection with the further consideration of FAC 84-10 and the Draft Final.

As requested by Mr. Rizzi, we have attempted to capture in writing the spirit and intent, if not the exact wording, of many of the oral comments and suggestions made by CBEMA representatives during the course of the September 10, 1985, Public Meeting. In addition, we are attaching to this letter the notes used as the basis of CBEMA's oral presentation in the early stages of the public meeting.

Our overriding concern is that we view FAC 84-10 and the September 4, 1985, Draft Final as an unwarranted regulatory overreach into the commercial product business. We would summarize our fundamental concerns in support of this position as:

- This regulatory action started with a legislative initiative to solve problems of alleged unreasonable prices charged to the Government by weapon systems prime contractors for commercial spare and replacement parts which the prime did not manufacture. It has grown from that initiative into a major procurement regulatory policy change governing the procurement of any commercial products directly from their manufacturers.

- FAC 84-10 and the Draft Final tend to take "cost-based" procurement policies, regulations and practices (which have governed the arena in which the horror stories have allegedly occurred) and impose them upon the free enterprise commercial product industry.

  Application of the certification requirements to all commercial products without limitation is simply not consistent with the intent of Congress. Indeed, Senator Carl Levin (D-MI) directly affirmed his understanding of this issue in an August 20, 1985, letter to DOD Assistant Secretary James Wade, Jr.:

  > "As you know, in these two statutes, Congress was attempting to address contractor overcharges to the Government for commercial spare and replacement parts which companies also sold to their commercial customers."

Computer and Business Equipment Manufacturers Association 311 First Street, N.W., Suite 500, Washington, D.C. 20001 (202) 737-8888

This member of the Congress was one of the original authors of these sections of the laws enacted in 1984. His statement contained in his recent correspondence is therefore directly pertinent to the Government's final determination on this critical question.

- The continued apparent intent to consider the United States Government as a commercial entity or as a part of the public is contrary to all accepted principles of law or regulation. Accordingly, the Draft Final must be modified to reflect the long-standing definitions of "commercial" and the category of "the public." Inclusion of Federal agency contracts in the reporting requirements of the certification is specifically inappropriate because the statute mandates its relevance on to "sales to the public." The Federal Government is not part of the legal or regulatory concept of "the public."

- With regard to these issues, there was also not an agreed understanding between the Government and industry at the Public Meeting with regard to the existence of substantive distinctions between the nature of the U.S. Government as a buyer and the nature of a wide range of commercial marketing and sales entities. This conflict manifests itself in the disagreement over the applicability of end-user prices to the Government as opposed to prices normally limited to OEMs, dealers, distributors, re-marketers or affiliates. These specialized business entities relieve a manufacturer of a variety of normal costs and responsibilities, including distribution, sales, administration, servicing and warranty of the subject products.

  The Government, as an end-user, does not perform these commercial operations and functions. Accordingly, the Government is entitled as an end-user to those prices transacted with the class of customer it most directly resembles, specifically that of commercial end-users. Moreover, these distinctions are also directly pertinent in helping define the differences between the Government and these business entities in that these channels and distribution chains expand the markets for a manufacturer's products and allow that manufacturer to reach customers to which he would not otherwise have direct access. Such functions are not within the scope of the role of the Government in the United States; accordingly, these categories of business customers should be excluded from this proposed regulatory coverage.

  To achieve these necessary clarifications, we strongly recommend that you adopt the corrective language recommended on page 7 of the CBEMA written statement submitted at the September 10 Public Meeting.

- We are still most concerned that there is a lack of clarity as to the application of the FAC. The statutes are very specific as to the requirement that contractors certify in those procurements using other than competitive procedures.

References in the Draft Final to "sealed bid acquisitions" and "(in) adequate price competition" significantly complicate the impact of the Draft Final and extend it substantially beyond its intended application. As such, the Draft Final is confusing in that it is inherently contradictory; if, indeed, the Draft Final is addressed (as in the law) only to procurement by other than competitive procedures, then the above-cited passages are incongruous on their face. In this regard, we believe that the final rule should stipulate that the clause shall not be included in solicitations when the contracting officer contemplates that he or she will receive two or more responsible and responsive bids. If that situation does not exist after responses are received, the contracting officer then specifically must notify the contractor that a certificate will be required, if not exempted for other reasons.

NOTE: Indeed, as demonstrated in the Comptroller General's decision in Sorbus, Inc., (B-183942, July 12, 1976, 76-2 CPD, 31), the Government is entitled to the lowest price that competition produces but not to a guarantee that the price will be lower for other agencies or under other circumstances. It is in these distinctions that the stipulations of the law become most significant in setting forth the legislative directive that in instances of the non-competitive acquisition of commercial spare and replacement parts, contractors are to certify that commercial prices offered to the Government not exceed "the lowest price at which such items are sold by the contractor to the public." To blur these several separate and distinct concepts together would greatly disturb competition and the Government's reliance on the marketplace.

o Any inference of requirements for cost or pricing data on commercial catalog items does serious damage to the Government's reliance on commercial products and the free marketplace. As such, the Draft Final will tend to drive the Government toward cost-based acquisition of all products and, through this, extend Federal regulatory oversight into the traditionally proprietary commercial practices upon which our economic system is based. Language should therefore be inserted at 52.215-32 (new d) as follows: "Nothing herein shall require the submission of cost or pricing data not otherwise required by law." This is language suggested by the Government at the Public Meeting and which its representatives indicated would be most seriously considered for addition to the final rule.

o With regard to the need to modify the price comparison time-frame provision to be used in considering the prices offered in the subject non-competitive acquisitions, the Government indicated at the Public Meeting that it would seriously consider use of the existing requirement contained in Standard Form 1412. If adopted, that language would read as requiring information for "...the most recent regular monthly, quarterly or other period for which sales data are reasonably available..." We strongly urge the

Government to indeed accept this suggestion. Adoption of existing Government contracting language relative to reports associated with a company's regular reporting period would dramatically improve the burdens imposed by the Draft Final on both Government and industry.

o The audit provisions must be clear and precise with regard to its application only to directly pertinent sales information to verify the veracity of a certificate. Accordingly, we strongly urge that the Government adopt the language which CBEMA proposed on this subject on page 7 of our September 10 written statement.

As discussed in the September 10 Public Meeting, the overall impact of FAC 84-10 and the Draft Final is to damage the underlying first principles which shape the relationship between Government and industry; this is the real crux of what is so seriously wrong with these regulations.

The first principles which are at stake go to the fact that in our economic system the Government is not a commercial entity, nor is it a represented component of the United States body politic, a part of the American general public. Rather, the Government, as an end-user, is the beneficiary of the market forces of free enterprise, which develop, price, supply, and service commercial products. The FAR clearly affirms these first principles, including the concept of Government reliance on commercial forces for the supply of standard products and services to the extent feasible.

Unfortunately, FAC 84-10 and the Draft Final rewrite the fundamentals of the relationship between the U.S. Government and the American commercial product industry. The enormity of the paperwork and administrative burdens imposed on industry by the Drafat Final as written, while representing a most serious consideration, actually pales in comparison to the negativity of its impact on the first principles of the basic role of the Government in its relationship with the commercial product industry and the free economic sector.

We ask the FAR Secretariat, the DAR Council, the Civilian Agency Acquisition Council, and policymakers at the highest levels in NASA, GSA and DOD, to reassess the unnecessary overreaching provisions of this FAC and Draft Final and to simply draft regulations which reasonably and equitably implement the mandates of the law by adopting CBEMA's recommendations. Once accomplished, these regulations could greatly benefit the public interest rather than cause serious damage to the delicate balance upon which we all depend.

We remain at your disposal to assist in resolving this critical matter.

Sincerely,

Susan G. Stuebing
Director, Government
Procurement Programs

Enclosure

CC: Mr. Stuart J. Evans, Assistant Administrator for Procurement, NASA
Honorable James P. Wade, Jr., Assistant Secretary for Defense for Acquisition and Logistics
Honorable Terence C. Golden, Administrator, General Services Administration
Mr. Robert P. Bedell, Acting Administrator, Office of Information and Regulatory Affairs, OMB
Mr. William E. Mathis, Acting Administrator, Office of Federal Procurement Policy, OMB
Mr. Alan R. Yuspeh, General Counsel, Senate Armed Services Committee
Mr. Alan L. Chvotkin, Counsel for the Minority, Senate Armed Services Committee
Mr. William B. Montalto, Procurement Policy Counsel, Senate Small Business Committee
Mr. John M. Duncan, Staff Director, Senate Governmental Affairs Committee
Ms. Colleen A. Preston, Counsel, House Armed Services Committee
Mr. William M. Jones, General Counsel, House Government Operations Committee
Mr. Stephen M. Daniels, Minority Staff Director/Counsel, House Government Operations Committee
Honorable James C. Miller, Chairman, Federal Trade Commission

Senator QUAYLE. Thank you very much, Mr. Henriques, and all the panel members for a very fine presentation.

As I sit here and listen to all of you, you have expressed some obvious concern. You have used the term "confusion," the problem of instability, the problem with implementation of the legislation.

I get the distinct feeling, and maybe you will correct me if I am wrong, that much of the problem is with the interpretation and the implementation of the legislation rather than the legislation, itself.

Am I correct in that or not?

Mr. HARR. I would like to answer, if I could, Senator.

We think that is right. You cannot back away from the fact that the legislation gives rise to the regulationmaking, but the question is whether the implementing regulations transcend, distort or obfuscate the meaning of the statute or go beyond it or pervert it.

I do not want this just to come from industry. I am glad it was said by the logistics commanders before this subcommittee. There is a real inhibition—there is inhibition in the implementing activities borne of fear, fear of publicity, fear the boss will be mad at them if he has been called to come before the congressional committee because of some horror story.

It grows with each layer down to where the rubber meets the road in many instances. So that is definitely part of the problem. I do not know how that can be gotten away from until we get on top—perhaps the best way to get on top of the authority is the talking which we are doing now.

We say and we have said in our statement that it is the implementation giving us the problem. It is people trying to be more Catholic than the Pope each step of the way down the line to be sure that they will not be later criticized. It is exaggerated in many cases.

Senator QUAYLE. Is that pretty much the consensus?

Mr. STEWART. No, Mr. Chairman. I would answer a little differently.

First of all, I do not want to demean the problem created by implementation and interpretation. We have had some examples this morning of overreaching in the process.

I would say this: There is too much legislation and the character of the legislation is too detailed in that it is contrary to the general historic function of writing a law, laying down principles, motives, philosophy and allowing it to be administered in more detail.

The Congress has been engaging in micromanagement—it has been engaging in specific disallowances of costs, for example. It is overdefinitive in its legislation and it is overproductive in terms of the number of bills that are generated.

So, I think it is a problem that must be shared and I would not accept the proposition that the problem is primarily interpretative and implementation in character, however important that side is.

Senator Quayle. Would you say it is primarily legislation?

Mr. Stewart. No, I would say it is a mix.

Senator Quayle. A 50-50 balance?

Mr. Stewart. It depends on the situation.

Senator Quayle. Mr. Rittenhouse is shaking his head.

Mr. Rittenhouse. That is how I come down: 50 percent too much, 50 percent difficulty of implementation.

I want to add another thing which Karl alluded to and that is the environment of fear, especially at the intermediate levels. I am talking both DOD, civilian agencies and the contractors.

It is one thing for me to sit down with the Assistant Secretary or the Secretary and negotiate, and we both, I think, have the best interests of the country at heart, and talk about a principle.

It is an entirely other thing in the environment of fear in which we are living for us to recognize that people in the chain will not move on some things until they get clear explicit direction from on high.

We are slowing down the process because they are waiting until the boss tells them the exact nature of the implementation of each of these statutes. That is the safest way they can go about it.

Like on the subject of too much legislation, they come back to this work standard issue and the Boxer amendment. I would like to comment specifically on that because I have a very large fear about that because it is such an anachronistic thing in our factory.

In our business we have one factory volume oriented and we make thousands of things there. In that one I will see like 6 percent labor content. That is all forms of labor. That is a factory which is making lots of things. So, it is the place which is most applicable in considering where I look at this.

I am talking about a defense factory now. I am looking really at 3 percent of the action. More important than that, I do not want to freeze into measuring touch labor. I want to get touch labor out and automate and use flexible production and other approaches and my goal should be to get touch labor down to 1 percent, not 3 percent.

That is the way we will be a world class competitor in the long run.

In the opposite spectrum we build satellites very carefully one at a time. We will get MIL Standard 1657 invoked on that and it will cost the Goverment money.

Out of that we will probably get a lot of good publicity. We have accepted it, we have worked with the customer. We have explicitly measured everything we have done and everybody will say what a good boy we are, but we will have forgotten fundamentally that we cost the Government more money to implement that.

I cannot stress strongly enough that I think defense is our current bastion on technology in this country. It is the place where we have opportunity to improve ourselves because that is where the focus is right now.

To put an anachronistic rule into place, I think is a step in the wrong direction.

Senator **Glenn**. Mr. Chairman, would you yield? I would like to ask unanimous consent we might be able to submit questions that will be included in the record so that they can respond later on in case they are not covered here.

I will try to get back.

Senator **Quayle**. That may be done.

Now let us talk about the legislation that has been introduced.

Mr. Stewart and Mr. Rittenhouse particularly indicated perhaps too much legislation.

What changes in legislation or repeal of legislation in the area of procurement should we be considering?

What I am looking for is a shopping list. We have gone in the direction in the past few years to more and more legislation. That is why we are having these hearings, it is time to slow the situation down, stop and take a look.

Is it more implementation than legislation?

I get mixed reviews here. I suppose it is both. Let us take the legislative side. We can deal with that directly.

Where would you go? What would you recommend to this committee to look at what laws have been passed that you would like to see repealed? What laws have been passed that you think need to be amended?

Or would you say, OK, the legislation is not really all that onerous, not that bad and we will take it, do not give us any more?

If you come down on that side, I will say the Congress will probably keep going in that direction.

Mr. Rittenhouse?

Mr. **Rittenhouse**. Let me comment on two areas.

First of all, any legislation that has taken judgment and discretion away from the contracting officer, not the program manager, but the contracting officer, I would say we ought to seriously look at that. That is one area I suggest you monitor closely with the idea that maybe that legislation ought to go——

Senator **Quayle**. Which legislation do you think does that?

You may want to submit it for the record.

Mr. **Rittenhouse**. I will have to submit it for the record.

Senator **Quayle**. I would like to see what legislation takes away authority and responsibility from the contracting officer.

Mr. **Rittenhouse**. Obviously, that legislation which invoked the work standards, touch labor, obviously, I know, should go.

I think what we can do for the record is research that and answer your question more specifically.

I think the advice from the panel this morning, what we have tried to communicate, is to stop what we are doing now and not do anything more while we ingest and measure what we already have.

I have to make this point. Not all of it is bad.

Senator QUAYLE. That is clearly what these hearings are pointing out. It is not all bad, but there might be some minor adjustments.

Mr. RITTENHOUSE. For instance, competition is a very effective tool to use to keep costs under control. As I understand it, there is more and more pressure coming, dual sources on all major programs, and we put an arbitrary number on them. I think it is $100 million.

That does not necessarily make sense. Somebody has to look at the total program, see what is involved, see what the cost drivers are, what capital it takes to push those programs and then make a decision whether it makes sense or not.

The outs that are allowed the various people within the services I do not think cover enough of the type of areas that make sense for competition. Competition is good, but it is not the total answer.

Senator QUAYLE. Candidates for repeal, modification, amendment.

Mr. Stewart, do you have any?

Mr. STEWART. I think you have gotten much too definitive with respect to disallowance of cost. It is too highly structured, much too detailed. You are really preempting the administrative side.

You had a go-around on the warranty situation. The first thing that happened was that the Congress enacted the Andrews amendment. Underlying that was a misunderstanding of the difference between the commercial sector, a relatively low technology product like farm equipment, and very high technology, exotic stuff that is produced in the defense system.

The Congress itself moved back and substantially corrected the Andrews amendment.

Senator QUAYLE. This subcommittee did.

Mr. STEWART. And I commend it for doing so.

Senator QUAYLE. Is the provision now adequate?

Mr. STEWART. It ought to be rechecked and carefully examined because underlying the much improved and amended version is the notion that you can transfer a commercial type warranty concept to high technology weaponry.

The law also calls for a mandatory warranty directive, subject to waiver. That ought to be rechecked in terms of whether or not the waiver language gives the Department of Defense sufficient flexibility.

Now, I give you one about which I feel very strongly. Part of the problem that you have in the procurement system now is due to the fact that you have an inspector general. This is not a personal criticism at all; I am talking about the role of the office.

The inspector general, in essence, is not a part of the procurement process. He is a creature of the Congress whom you created in your own wisdom for the purpose of looking over the shoulders of the procurement process, particularly with regard to fraud, waste, abuse, and so on.

That is a problem in the sense that it gives separate, strong authority to the inspector general who really has no procurement responsibility whatsoever. He is not primarily interested in the procurement process except to the extent of finding abuses, and so on.

Senator **Quayle**. Should we repeal that?

Mr. **Stewart**. You should reexamine it in terms of the relationship between the procurement process and the separate creature of an inspector general.

Senator **Quayle**. Redefine his role and responsibility?

Mr. **Stewart**. Correct.

Senator **Quayle**. Other candidates?

Mr. **Harr**. The work measurement standards would be one.

Senator **Quayle**. That has not been signed into law, but it has gotten a lot of attention.

Mr. **Harr**. I do not want to be facetious, but in my view, all 21 provisions of the Defense Authorization Bill of 1986 are unnecessary. One in particular, the DCAA subpoena power, stands high on the list. That should be amended.

I want to correct the record a little bit, if I may, Mr. Chairman. I still disagree with my esteemed colleague, Charlie Stewart, as to the balance of blame in terms of the confusion that now exists in the procurement environment.

I still put the primary emphasis on excessive implementation. I would not exonerate, with all due respect, the Congress.

Senator **Quayle**. Mr. Henriques?

Mr. **Henriques**. Again, Mr. Chairman, we are coming from a slightly different angle because we are talking of commercial products. I think the current legislation could be amended to make clear the need for distinction between commercial and cost-based products.

Within the operational aspect on implementation I tend to agree more with Karl that the implementation is more dangerous than the legislation certainly.

We would suggest that the open rulemaking process could have this kind of set of options; maybe, specify in the legislation dates by which the proposed regulations must be issued for public comment rather than, or perhaps in addition to, the dates by which the regulations must be in effect, and then to suggest that the waiver provisions of section 22 of the OFPP Act be amended, or limit the waiver provisions, so that they are invoked only if the legs are not reaching beyond the scope of the statute.

For example, after your subcommittee dealt with the warranty issue, the commercial warranty exemption which was put in, we thought was very valuable.

Finally, there is one other thing that has to be looked at in regard to the basic underpinning problem of defense procurement. We want a strong industry to support the Defense Department and to support the country.

We are concerned that in the commercial product area, again, the cost of reporting requirements that are being levied on the industry with all of the new sets of laws is such that it is going to put us in a less and less competitive position internationally and if that happens, we cannot support the industry the way we should.

If we cannot support it, we will be followers and not leaders in the high technology area.

Mr. STEWART. Mr. Chairman, may I amplify a bit for a second? I think there is another thing that should be pointed out. We made the point that various procurement objectives sometimes have an inherent conflict. When you legislate for socioeconomic reasons in the procurement area in order to accomplish a small business or minority objective, and then you tie into that objective proprietary data requirements in order to facilitate the transfer of contract business from experienced contractors, and so on, you are creating a problem with regard to the process.

I think that one of the suggestions that I would restate would be that the Congress examine this body of legislation and test each provision against the basic objectives that you are trying to accomplish.

The funadamental one, of course, is high quality product, reasonable cost, and timely delivery. So, I think there is an overriding problem here.

There is another point with reference to this question of who is to blame. A part of the difficulty with reference to this environment that we hear so much about is the fact that any administrator of a department such as the Department of Defense has to read the mood of the Congress.

The mood of the Congress in this area is clear, supercritical, overlapping of statutes, specific directives to administrators going beyond the normal statutory purpose, and the Secretary of Defense reads that mood and he responds. He spends too much time trying to tell the Congress that he found out about something before your subcommittee investigation found out about it.

I think really that there is a malaise, a mood that is created by the statutory process that is reflected in the administrative reaction.

Senator QUAYLE. Chairman Goldwater?

Senator GOLDWATER. This is some of the best testimony I have heard on this subject. I can tell you that for the industry it is long, long overdue.

I have to remind you not of the peculiarity, but the nature of our media. You will see news essentially on the front page of the paper. You see something on it that will sell that paper. They have the same problem you have. They want to sell papers. You want to sell your product.

So, every time somebody makes a little mistake and pays $400 for a hammer or $600 for a can, it is all in the front page of the newspaper and media. The American people say these people are getting rich off what we are spending on defense.

They overlook the fact that we produce the finest weapons made in the whole world; we produce the finest of everything. I am saying that to you so that you can be particularly more careful in the days ahead.

Now, you mentioned 3,000 personnel involved in getting spares; 87,000 civilians around this town trying to help the military and they are not doing a bit of good.

I think the Congress is to blame. Congress has tried to micromanage business. I think there are 13 people among the hundred Members of the Senate that have ever been engaged in business.

So, we are getting into things that we do not understand. The budget for the military is over $300 billion. We sign 15 million contracts a year.

I am just mentioning these to give you some kind of an idea of what we are up against. We spent almost 3 weeks this summer on a conference with the House on the armed services bill.

You will not believe this, but most of the time was spent on what we call the revolving door or what is the poor guy going to do when he wears a uniform and most of it was on the very subject you have been talking about, amendments that want to restrict, restrict, restrict, restrict.

We even have the House of Representatives now violating all concepts of parliamentary procedure with the Speaker insisting that five of these items that we decided against in conference come back and be on the appropriations bill, and the Boxer amendment is one of those. I think we have that shot down.

I did not want to make a long statement on this, but this testimony is very good, I just had to comment on it. I hope it gets good, wide circulation among the business people of this country. There is no need for you to have to put up with what you put up with.

I can tell you that the military services, each one of them, are now engaged in their own improvement in management. I do not think they are making the kind of progress they would like to make, but they are making it.

When we can produce a weapon like the B-1 under cost and ahead of schedule, I think it is an indication of what we are getting down to.

When we built three cruisers last year from money saved by competition, that is the kind of thing we are getting to and we have to depend on you fellows in business.

Mr. Chairman, I apologize for making a long speech, I do not believe in them, but I got here late the wrong time and heard the right things and that, thank God, somebody finally said it.

I thank you gentlemen for coming here. I happen to be a businessman, myself.

Senator QUAYLE. We appreciate your statement, Mr. Chairman.

Senator Levin?

Senator LEVIN. I am a little reluctant to even ask my technical question after Senator Goldwater put his finger so succinctly on it.

You know, this work measurement standard is a typical example of what the problem is legislatively. You have something that is going to be signed into law. We have never had a hearing on it in the Senate. I do not believe the House ever had a hearing on it before they passed it.

We have been trying to amend it, we are trying to delay it, we are struggling to prevent it from coming into existence. The chairman has been leading an effort which I totally support to see if we cannot at least delay this thing until we can have some hearings on it.

I understand what kind of beast we are creating, what kind of paperwork we are requiring, but the taxpayers will have to pay for it. It does not come free. We are caught in this bind that, as a matter of fact, a slightly watered down version is going to become law as soon as the President signs the authorization bill.

There is a bill that I have introduced to try to soften the blow, Senate bill 1783—I hope you will take a look at it—which would delay it, which would clarify the language to make sure we do not require either the contractor or the Defense Department to record this stuff if they do not already do it.

That is the critical issue because the way the Defense Department reads this language, they are reading that we are requiring them to record this information even though the contractor does not. We will have the Defense Department sign contracts with all kinds of experts to measure stuff which is not useful to anybody.

A companion bill has already passed the House, I believe, making clear that the only time we are going to get this information or require DOD to record it is where the contractor is already doing it on his own which would clarify some of the problem, at least correct some of the problem.

At any rate, it is a complicated issue.

I do not want to spend all my time on that, although it is a good example of how we make bad laws. It is much more complicated than even what I have tried.

If you have not already taken a look at S. 1783, I wish you would and give us your reaction to it.

One of the statements the chairman said I want to comment on and support. He is soliciting from you folks a wish list of legislation you would like to see amended and repealed. Each one of you has tried to give us one or two examples.

I know, if he has not already said it, he would concur, that we solicit for the record a specific list of legislation that gives you trouble so that we can look at it. It is very important that we be precise. We know you are overloaded with regulations and laws that are coming so fast, the changes are coming so fast you cannot handle them.

We understand that. We understand the problem with the work measurement standard. A day does not go by when Senator Quayle and I are not discussing strategy for getting around a bad law. That we have a pretty good handle on, we think.

There are a lot of others we would like your help on. We would solicit your specific recommendations on it.

In a lot of things you are in agreement. In other things you are in disagreement. Right on this panel, to show how complicated our life is, somebody said legislation is too detailed—Mr. Stewart. Too definitive. Mr. Harr said the problem is administrative overreach.

One of the reasons we get administrative overreach is because there is not enough direction from the Congress. That is one of the reasons. There is also a natural instinct to overreach. That is a part of the beast, too.

Putting aside that natural instinct, the more general we are, the more likely it is that the administration is going to fill in the gaps.

So, there is a conflict there. Do we micromanage the bills? Do we write these bills in tremendous detail going into great specificity as to what items can be charged for and what cannot?

You cannot charge for beer with an alcohol content of 11.8 percent or more; if it is low alcohol beer, you can. That is about where we have gotten. If we do not do that, God willing we will not, the administrative overreach will be a lot greater.

So, to some extent I think you realize that the more general we are in our laws, the greater that overreach will be, not that there will not be overreach otherwise.

To some extent there is a difference among you as to how specific we should be in these laws. Sometimes we are general for political reasons, we do not want to handle a hot issue, so we write it general to get consent. Other times we write it for better reasons, so that we should micromanage.

So, there are good and bad reasons to be general. In any event, there is conflict here which is understandable. We face that every day as to how we get legislation done.

I have a number of specific questions, but before that, I want to make one other comment.

I think it was Mr. Stewart also who said to decide who is in charge. I believe he said, God knows, how many audits, 47 separate audits, I think he said, Government audit functions within his company.

Who is in charge?

By the way, I sympathize with your dilemmas, problems, and costs. Essentially, this Government is based on a check and balance between the branches, between the Congress and the executive, within the branches, within, indeed, the services, that we know when we look at review organizations of the service we do not know who is in charge of the service.

In lots of ways we do not. We have four services who are in charge to some extent. We have a check and balance between the House and the Senate. You are going to get audited probably by both. Within each branch you are going to have it, Republicans check on Democrats and vice versa.

That is just within the Congress. Between the Congress and the executive you are going to have a check and balance just as the Constitution says. There will be built-in checks and balances which will create nothing but cost for you folks.

Even if we can reduce the numbers, there will be some built-in duplication and overlap because that is the system we created here that we do not have any one person in charge.

In the Congress we could never do what you suggest, have one line that everybody agreed to, because we check each other to make sure when the House messes up, which they do regularly, that we correct them, which we do regularly, and vice versa.

So, do not be too idealistic and enthusiastic as to how much reduction in overlap we can get.

I wish I could give you a better answer. I do not rely too much on that. That is not where the relief is going to come from. Your relief is going to probably come from a different place of structural change.

Now, I want to get to another point. I think to some extent the industry is going to help and regulate itself, particularly in the areas which create all kinds of public relations problems for you.

You have to find a way, I believe, to address the Allen wrenches, toilet seats, and the ashtrays.

Take the ashtrays. There is a logic behind that cost. I forget what the cost was. I think we asked for 10 ashtrays for 5 planes. Some company won out and got blueprints from us and had to create 10 of them. They have to tool up and create them. It cost a fortune to do it.

There was logic behind it. So what? If you rest comfortable because it is logical, you will not make a mistake. I assume there was logic behind it. So what?

The public is going to read and hear that some ashtrays cost $1,012. Or was that the Allen wrench, $9,500? You see, my staff is here to check me.

They are going to read it. It is true. Should it have cost that? You will find out a month later or 2 months later that it should have or it should not have or why it did. By that time credibility will be eroded a little bit more.

I believe the industry has to come up with a mechanism to act quickly on problems which are raised by a no-question-asked monitor.

Let me rephrase it. Someone monitors the industry at its own effort that reaches a 48-hour decision, no questions asked, or something similar, to address the perception problem that you folks have and it is going to corrode the Defense Establishment and the budget around here.

You are going to continue to have it because we are going to continue to buy spare parts. We are going to continue to face the problem you talked about where we are going to buy them on a cost basis of some kind instead of competitive basis.

We are going to continue to buy some things on a noncompetitive, commercial basis. Whether it is a 30 or 40 percent, whatever it is, we are going to have to continue to buy those. It does not make sense to buy them any other way.

We will continue to face this problem, continue to have stories come out about the cost of that process. We are going to continue to try to cure that problem legislatively which in many cases contributes as many headaches as solutions.

All I am suggesting to the industry is that I think you have to figure out a way to address the problems that are raised dramatically in a way which may not be logical, but which is fast and gives relief and is done by a credible person so that the analysis does not come out 6 months after the story.

When you get the story of that pencil which cost $48, I would like to go to some monitor and say, "OK, you are with the industry. That pencil cost $48. What is the reason? What is the answer? Give us a solution quick."

And that person may say in 48 hours to your folks, "Does that pencil cost $48? Do you know why it did? Because that is a brand new eraser, a graphite-free eraser that caused so much trouble. Tell the Government they have 480 bucks, 10 pencils times 48. It does not make any difference. Figure out some pool to pay those things out."

I am thinking out loud and perhaps off base. All I am suggesting is if it is not that solution, folks, if you were physicians, I would tell you heal themselves. I tell you that you have to help us come up with a solution that produces credibility in areas that are creating problems for you in two ways.

No. 1, it undermines credibility in the budget and the size of the budget and the whole Defense Establishment.

Second, it produces legislation that you are unhappy with.

Both ways it creates problems. I urge you to come together.

If I have one minute left, I will ask questions.

This question goes to Mr. Rittenhouse. It has to do with the DOD implementation of a regulation, the lowest commercial price regulation. I am interested in this area for other reasons, not just my current hat I am wearing on this subcommittee.

You say that the OMB here disapproved the regulation on the basis of its content rather than form.

Will you tell us how that process works?

Mr. RITTENHOUSE. On this one I will have to ask for some help from my compatriots from EIA.

Let us respond to that for the record.

The basic issue is that the new recordkeeping requirement was so burdensome, it was not the cost of implementation.

Senator LEVIN. If Mr. Henriques could answer that, although I am fairly well over my time. I ought to make long speeches more often.

Mr. HENRIQUES. I can give you a fairly brief answer and then I will supply one in more detail.

The original intent of the legislation as it appeared was to talk about the spare parts cost and then it was extended to commercial customers.

In the regulation this became extended to all customers, not just commercial customers. There are relationships that exist between original equipment manufacturers, dealers and, in fact, Government agencies which were not appropriate for the data that is being demanded to be collected.

It creates a really egregious overburden of administrative cost to maintain this kind of thing. The audit provisions and subpoena provisions, and so forth, appear to be totally out of line with the intent of what your committee said and the conference committee said.

Senator LEVIN. What was OMB's role?

Mr. HENRIQUES. OMB in reviewing this said that DOD had not established a case for demanding that kind of data and said do not issue the regulation.

Senator LEVIN. Were they willing to meet with you on that?

Mr. HENRIQUES. Yes.

Mr. STEWART. May I comment, Mr. Chairman, on a conflict that Senator Levin referred to, namely, the question of whether you are too specific or too general, and so on?

I do not think there is as much need for reconciliation as you might think. Let me give you an example.

When the Congress addressed the warranty issue, it really faced the first question which is whether or not the Congress should legislate a warranty requirement as a statutory mandate. That was the first question.

On my standard with regard to simplicity of statute as distinguished from detailed law, I would have answered that no.

The Pentagon was already well into warranties where they were appropriate. There was no need for it, but when the Congress legislated a mistake in terms of the contents of the provision, it had to be cleared up by more detail.

So, I do not have the same difficulty with the question as to whether you should be detailed or general that you seem to have.

Senator QUAYLE. Senator Bingaman?

Senator BINGAMAN. Thank you, Mr. Chairman.

Let me just shift discussion to a slightly different area.

I think there is a growing view here among some of us who have been looking at this area that at this stage perhaps the best thing that the Congress can do to deal with procurement problems is to focus on the personnel side in the Government agencies that interface with industry, the procurement personnel, scientific, personnel, and try to upgrade the qualifications and experience of all the people who are actually making the decisions.

One way to deal with management problems instead of micromanaging and passing all kinds of detailed legislation and having all kinds of oversight hearings is to put people in there whom you feel have the competence to deal with it in a managerial sense and then hold them accountable for doing so.

I would be interested in your reaction as to whether you think that is part of the solution or a large part of the solution and then, second, if you do think it is part of the solution, would you have thoughts as to how we should go about up grading the personnel who are involved in this procurement process?

Does anybody want to react to that?

I am not trying to get you to say critical things about the people you have to work with on a daily basis. I an just saying if your suggestion that we should consult industry early before we make policy is a serious one, I am telling you we are likely to make policy in this area next year.

I will be interested in knowing what industry's reaction is.

Mr. HARR. You cannot underestimate the importance of the quality of the people in the process, obviously. We would agree, certainly to the extent to which that is a truism, anything that can be done will be helpful.

On the same point, upgrading the personnel quantitatively would be a negative as far as we can see There are probably too many people in this business now.

Let me go back, if I may, to a rough analogy I made between a good team and the situation we find ourselves in now.

Sure, one of the ways to improve performance is to upgrade quality, but much more practical, I suppose, in the immediate area is make sure they get trained. Training is a function of time, organization.

When the volume of upcoming directives, be they legislative or regulatory, is too great and too fast, you send an untrained team out there in the field. If it was a choice between those two, we would probably feel that allowing adequate time to digest the laws and regulations in the form of training time would be more important.

We do come down awfully hard on the implementation process in our statement, and we have to be candid with the subcommittee. However, the fact is we recognize some of the best people are in the Government procurement business.

We are not talking about incompetence or ill will or venality or anything like that. We are talking about an insuperable problem under circumstances which are very frustrating.

I do not have any specific ideas or specific steps to upgrade the quality.

Mr. STEWART. If your objective is to achieve the highest quality corps of people in the procurement process, you not only do it by selection, by training, by incentive programs, but you also try to avoid such matters as loading the process by statutory directive with people who are called by some of the individuals I quoted as checkers, as distinguished from doers, to the point where the contracting officer no longer has any incentive than to protect his own hide.

He does not become a better man under that system; he becomes a weaker man. So, I think you have to look at not only the training and selection, but you will have to look at the conflict between the layers that you create by procurement statutes.

Now, returning to the question that you were directly addressing, namely, upgrading the corps. There is a professional organization called the National Contract Management Association. It is not a spokesman for industry. It is a professional organization made up of people who are in the contracting business, in the Government as well as in the private sector.

They have a very elaborate training program and aids to training in order to bring along a professional corps in this field.

I think the staff might want to consult with them in respect to your very significant question.

I repeat, do not overlook what you are doing to morale, what you are doing to development, when you create a system which almost wipes out the initiative of a contracting officer or a project manager and puts them in a chain which makes the auditor the ultimate decisionmaker in every case on subjects where he really is not capable of making a contracting decision.

Senator BINGAMAN. Does anyone want to comment?

I appreciate your thoughts.

That is all I have, Mr. Chairman.

Senator QUAYLE. Thank you very much, Senator Bingaman.

I have just one other question.

What kind of advice would you give to the Packard Commission as they come up with some procurement reforms?

I think Senator Bingaman has taken a strong interest and I have, as a matter of fact, cosponsored his bill to look at the personnel matter.

Would you advise the Packard Commission that when they look at procurement that they look at the people problem or should they focus on people and the process?

What would be your advice and counsel to them and where do you hope, for the sake of a better procurement situation, that they might come down?

Mr. HENRIQUEZ. I do not think it is an either/or situation. The substance of the law and the regulation, the process by which the procurements are made, and the third is the personnel. I think they are inseparable. I think you have to look at all three pieces of it, the substance, the process by which procurement is done and the personnel who do it.

Senator QUAYLE. So, you would hope that the Packard Commission would deal with all three and make specific recommendations.

Does the rest of the panel agree?

Mr. HARR. We have already made our suggestions to the Packard Commission and they did not include anything on personnel.

Senator QUAYLE. They did not?

Mr. HARR. They did not.

Senator QUAYLE. Do you think we should look at personnel?

Mr. HARR. Yes, I do. We think the one fundamental thing that stands out in this whole business as the clearest target for attack and improvement in the system is to delineate responsibility.

Senator QUAYLE. That is more process-oriented?

Mr. HARR. Yes; give the guy the job and make him do it, penalize him if he does not do it. Let him know he has the authority.

Senator QUAYLE. When you talk about "the guy," you are talking about the contracting officer?

Mr. HARR. I am talking about the contracting officer and the guy in industry.

Senator QUAYLE. You think we also should take a look at personnel?

Mr. HARR. Yes, indeed.

Senator QUAYLE. You might want to file an addendum to let them know that personnel is a strong interest because I think that is the direction I am going in and others have taken a lead.

Senator Bingaman is very interested in that and it is a key proponent of any procurement package.

Mr. RITTENHOUSE. I would like to say that I place that at a distance, personally.

Senator QUAYLE. Personnel?

Mr. RITTENHOUSE. Yes.

Senator QUAYLE. What would you put first?

Mr. RITTENHOUSE. I think I would take a look at the process itself and delineation of responsibility.

I would like to make a few comments contrasting where we are now with, say, 5 years ago to show you how the process and how the organizational authority have changed.

If you worked in a major weapons system 5 years back, you worked with the Government program manager, usually a military type. He was answering questions of the Congress, coming over on the Hill answering questions about his weapon system.

He had a check and balance with the contracting officer. They worked together, but generally our central authority figure in our major weapon system was the Government program manager.

When we work a major weapon system issue now, like do we need an improvement to stay up with the threat, a new power structure has emerged within the various secretariats. We are dealing with the Secretary or Under Secretary in discussing those issues as well as the program manager, as well as the contracting officer.

Because these things cost big dollars, we get questions from congressional subcommittees. We answer those in the spirit that we may as well give the best input we know how to give.

What we are getting is really trying to field out a lot of information to a lot of different places.

I make no inference these people are not well intended; I happen to believe they are.

Now, we are working for different bosses. That is why I asked, who is in charge?

And getting back to the point I made in the paper that addresses organizational structure and process, I am not naive enough to believe we do not need checks and balances, that the Congress is not going to exercise its authority to overview and that sort of thing, but I have to come back to the point of delineation of authority within whatever organizational structure you propose.

Frankly, I thought about this a lot personally and decided I am not wise enough to recommend exactly how that should be. There are a lot of different issues beyond just contractor issues involved in that.

To me, organization, process and people are important, but, and this will sound self-serving as a plug for the people we work with, I really haven't found that the quality of the people is a basic issue. I really do not have a hangup with that.

Senator **QUAYLE**. In general terms, speaking of the process, would you think your recommendation would be more for a centralized process or would you rather see the decentralizing concept accelerated?

Mr. **RITTENHOUSE**. I think where we are now we need a strong central authority to get rid of the multiple process. I am almost at the point where I really do not have a great deal of preference for where it should be.

Let us just define who is in charge and get on with it. I think if we are all interested in our country, which we are, then we will make good decisions under it.

Senator **QUAYLE**. If you centralized it, would you run a risk of having another boss on top?

Mr. **RITTENHOUSE**. I addressed that specifically in the paper with the added statement that says, "please just do not set up another one and add another boss to the process".

Senator **QUAYLE**. That is sort of a risk you run as you move toward decentralization.

Mr. **RITTENHOUSE**. It is very, very difficult. I do not have profound or sage advice on how to do that and detune some of the other power structures that have arisen.

Mr. **STEWART**. I do not think the division is as sharp as your questioning implies.

I would say as a general proposition in private industry or Government if you have a good organization, if you have a good system, if you have a good incentive program, the people will be attracted to that system, will develop under that system and will stay with that system.

We are now in the process, to repeat the point, of destroying the contracting officer corps. You do not make good people by that sort of approach. So, that I do not draw this sharp distinction between the process and people. I think they go together necessarily.

With regard to centralization, I made a point in my statement with respect to the fact that the services were running a little bit loose. I will give you an example.

On October 25 the Deputy Secretary of Defense issued an order, not a memorandum, although it is called a memorandum, and he said in his letter to the Secretary of the Navy.

"I appreciate your Department's attempt to provide additional guidance to your contracting officers concerning per diem cost allocable to DOD contracts. However, in this instance the procedure used by the Navy is not authorized under the existing Federal acquisition regulations.

"Therefore, you are requested to direct the Assistant Secretary of the Navy, Shipbuilding and Logistics, to withdraw the memorandum," which was the subject of this document.

Now, we have theoretically a centralized system with the OSD in charge. He has not been exercising that authority sufficiently.

Senator **Quayle**. Senator Levin?

Senator **Levin**. I just want to add one comment.

There was a conversation about Senate bill 1783 which addresses work measurement provisions. It was apparently reported as being a House initiative.

There is a companion House bill, as I indicated, which has been passed.

The facts are S. 1783 was introduced by me the day before the companion House bill was introduced. It was introduced by me in order to correct, modify, and repair the language in the Authorization bill relative to work measurement provisions. I do not like those provisions. Obviously, the chairman does not either.

We would like to repeal them. We cannot get a repeal, we do not think, we cannot repeal. When I proposed a bill to key House members on this issue to do three things, they accepted it.

You folks have to decide whether you think that is an improvement over existing law. I do.

I want you to know the origin of this was mine. It was my bill. I wrote it in an effort to modify, correct and repair the language in the Authorization bill. It was introduced in the Senate the day before it was introduced in the House. The Boxer bill, so-called, companion bill, was introduced after.

The bill would do three things. It would delay these provisions for 6 months. It gives us a chance to hold hearings and maybe repeal the darn thing.

Second, and this is the critical part to me, it states that if a contractor does not record this information, that DOD does not have to record the information.

That, to me, is the critical part. That is why I wanted to make it clear we are not imposing some new burden here where the material does not already exist. We will not require it be obtained by DOD or anybody else. That was the part that I got.

The part that the House got was that they would apply the requirement to existing contracts where again the contractor already recorded the information.

Where this information already exists, I do not mind making it available to DOD. What troubles me is requiring it to come into existence where it does not exist. That is what Senate bill 1783 would make clear it is not required.

I wanted to give you the origin of that because I think it is important, as to your response to it, that you understand that this is something I felt very strongly was needed to correct some of the portions of the authorization language in this area that I did not think made any sense. The House did get their language in there that would then apply to existing contracts, I do not think that this in any way creates the problem, the way the other part of the authorization language does, which would impose a new requirement that does not already exist.

If you will look at that with that background and let us know. If I can solicit on behalf of the chairman what your feelings are about Senate bill 1783, I would appreciate it and I think other members of the committee would.

Senator **Quayle**. I would concur. I think you have made a good attempt to try to correct it.

I still have not immersed myself into this bill, but I have worked with him in the past and I know this is a genuine effort that may be satisfactory to you.

That is what he is asking. He wants your comments. I tell you, quite frankly, we were blind-sided on this issue, to begin with. In the Senate it never should have gotten in, but it did. It got into the House.

We wrote as disparaging conference report language as we possibly could trying to point out the problems with it. This issue is now back.

Gentlemen, thank you very much. It has been fine testimony.

Our next hearing will be on November 13.

I might remind you the record will be kept open and I want that wish list of things you wanted modified, repealed, et cetera, because we need that as we look at some of our oversight responsibilities.

[The questions submitted by the Senators of the Armed Services Defense Acquisition Subcommittee to be answered for the record follow:]

QUESTIONS SUBMITTED TO MR. RITTENHOUSE, EXECUTIVE VICE PRESIDENT, RCA AEROSPACE AND DEFENSE ELECTRONIC INDUSTRIES ASSOCIATION

RCA,
Cherry Hill, NJ, December 4, 1985.

Hon. Dan Quayle,
Chairman, Suocommittee on Defense Acqusition Policy, Committee on Armed Services, U.S. Senate, Washington, DC.

Dear Mr. Chairman: Thank you for the opportunity to present the views of the Electronic Industries Association on the effects of recent procurement reform legislation. In accordance with your staff's request, I enclose a corrected transcript of my testimony at the November 7 hearing.

During the hearing, a number of questions were posed which I agreed to answer for the record. EIA has drafted a response to some of them. I enclose a copy of their response as well. I would greatly appreciate your including the EIA letter in the record of the hearing.

The following discussion is my response to the questions stated and those submitted later by Senators Dixon and Glenn.

QUESTIONS SUBMITTED BY SENATOR DAN QUAYLE

Senator QUAYLE. What is your reaction to S. 1783?

ANSWER. I strongly support S. 1783. It is an excellent interim response to the serious problems caused by the new "work measurement" statute. I view it as only an interim response, however, because I believe that the work measurement law must be repealed. It mixes apples and oranges by providing for measurement of a defense contractor's performance under standards derived for commercial work. Because military production specifications are vastly different from commercial specifications, in a variety of ways ranging from tolerances permitted to the manner of testing, commercial standards are meaningless when applied to defense work.

Secondly, as I said at the hearing, "work measurement" is an anachronism. Contractors engaged in high technology work are moving rapidly away from the types of manual work measured by such efficiency standards. Today, efficiency is not measured by how little manual labor is involved, but rather by how much scientifically controlled and computer assisted design and manufacturing goes into an item. Work measurement is an exercise which will cost the Government a great deal and produce very little usable data.

Senator QUAYLE. OMB disapproved the lowest commercial price regulation on the basis of its content rather than its form. Will you tell us how that process works?

ANSWER. OMB's review of regulations is accomplished to ensure compliance with other statutes such as the Paperwork Production Act. In this case, OMB's review demonstrated several major flaws in the DOD proposal. First, the regulation would have established extensive recordkeeping requirements which burdened both the commercial as well as the defense segments of the contractor's business. OMB determined that no need was shown for this burden, and disapproved the regulation for that reason.

Second, OMB questioned the regulation's establishing a means of auditing the commercial price being offered. Aside from verifying that the price is the lowest commercial price, an audit of such prices is a non sequitur.

Senator DIXON. What acquisition legislation currently in effect would you like to see modified or repealed?

ANSWER. I proceed from the assumption that if we ask for more legislation, we may get it. More legislation is the last thing we need. Nevertheless, several recent actions should be repealed at the earliest opportunity. They are:

1. WORK MEASUREMENT

As discussed above, this statute will cost the Government far more than the value of any data it will generate.

2. RESTRICTIONS ON CONTRACTING OFFICER DISCRETION

There are a number of provisions which tie the hands of contracting officers and preclude them from conducting their business functions more efficiently.

(a) Waivers of performance warranties

The requirement that DOD report to Congress on each case in which it waives the requirement for a performance warranty on a weapons system is not practical. Few, if any, program managers or service secretaries will be willing to find out that a warranty is not cost effective if he knows it may result in an invitation to defend that finding before a Congressional committee. Warranties should be required, but DOD's ability to make realistic determinations of their cost should not be hamstrung by the reporting requirement.

(b) Preclusion of settlement of indirect costs without the opinion of the defense contract audit

This provision of the 1986 Defense Authorization Act gives the auditor a veto over any portion of a settlement he disagrees with, regardless of how strong a case the contractor's auditor presents in favor of its allowability. No contracting officer will be able to accept a varying opinion because the language will be read to require a favorable auditor's opinion. Contracting officers should be required to obtain the advice and assistance of auditors, not bow to their every objection.

(c) 10 U.S.C. 2317 and section 502 of the Small Business and Federal Procurement Competition Enhancement Act of 1984

These laws require that contracting officers' personnel evaluations reflect their success in increasing competition. Every contracting officer is responsible to follow the law of acquisition. But their judgment should not be shackled by basing their ratings, and thus their promotions, raises, and bonuses, on artificial goals for competition.

3. PRESUMPTION OF COST REASONABLENESS

One provision of the FY '86 Defense Authorization Act reverses the longstanding presumption that a cost incurred by a contractor is reasonable. Under the *Bruce Construction* case, once a contractor had proven that it had incurred a cost, the burden of proof shifted to the Government to show that the amount was unreasonable. The FY '86 Authorization Act reverses this case.

Disputes over contract costs have always been governed by the "prudent businessman" test. The law assumed correctly that a prudent businessman, seeking sales in a competitive market, would only incur costs which were reasonable and would not damage his competitive standing.

Reversing the presumption of reasonableness will only serve to expand the demands of auditors and increase the litigiousness of both contractors and the Government in resolving disputes. It places the decision on reasonableness in the hands of the auditors rather than the marketplace where it belongs.

QUESTIONS SUBMITTED BY SENATOR ALAN DIXON

Senator DIXON. Gentlemen, you each devote a large proportion of your statement to concerns about the manner in which the Department of Defense has implemented the 1984 defense procurement legislation.

To what extent have the difficulties that you describe resulted from lack of clarity in original legislation in such areas as definitions, scope of coverage, et cetera?

ANSWER. These difficulties arise in only one sense from a lack of clarity in the statutes. In many instances, such as the warranties reporting requirement discussed above, Congress has attempted to give DOD flexibility in implementing its mandate. But Congress never seems to realize that by including reporting requirements on warranties waivers, amounts of competition, or auditors' savings, it creates tremendous pressures on DOD to follow the letter of the law and not its intent. Do away with most of these reporting requirements and many of the problems will disappear with them.

Senator DIXON. What specific actions do you recommend that we take to introduce additional clarity into the legislation enacted over the past two years?

ANSWER. Beyond the removal of superfluous reporting requirements, no new legislation is needed. Instead, this subcommittee should continue its oversight of DOD's regulatory implementation of the new laws. When it is clear that your intent is not being implemented, the subcommittee should indicate its displeasure to DOD. In most cases, this will not require more legislation.

Senator DIXON. Mr. Rittenhouse, in your testimony you state: "We believe that it is incumbent on Congress to ensure uniform, concise and timely dissemination and implementation of legislative reforms."

This sentiment has been echoed by all the witnesses here today.

What specific actions should this subcommittee be considering to achieve this goal?

ANSWER. The subcommittee should review the effectiveness of the Federal Acquisition Regulation mechanism. Ask your staff to survey the wide variety of regulations governing civilian and defense procurement. Ask them to compile the hundreds of variations within DOD and to determine how wide the variations are. Then ask DOD why so many variations exist.

The subcommittee should try to put some strength into the FAR process to minimize these numerous variations.

Senator DIXON. What steps can be taken to involve the industry and other affected parties at the front end of the rule-making process without adversely affecting the need for timely implementation of legislation?

ANSWER. This question must be answered in terms of your definition of "timely implementation." In most instances, DOD has been given six months or more to implement new legislation. Nevertheless, as in the case of rights in technical data, it has consumed over a year on internal drafting, leaving a month or less for industry comment.

One way to streamline DOD's implementation would be to have it invite industry proposals for implementation prior to issuing a proposed regulation for comment. DOD could then have the benefit of industry counsel from the outset, and should abbreviate the time now consumed in its own drafting.

Senator DIXON. Every one of you have underscored the need to emphasize quality in selecting sources for defense products. There seems to be a general perception that competition is now being based predominantly on price considerations to the detriment of quality.

What specific actions should we consider to more properly balance concerns for cost and quality in defense acquisition?

ANSWER. The emphasis on competition for its own sake is causing a decline in quality and is extending the time necessary to complete contracts.

One means of emphasizing quality would be to grade contractors on performance. Points should be given for exceeding contractual quality goals and performance standards. When a contractor competes for an analogous new contract, these points should count in its favor and directly offset the difference between its price and a lower offer in proportion to the benefit the Government obtained on earlier work.

Senator DIXON. How should we define quality criteria so that the wisdom of making a contract award on the basis of quality rather than price is readily apparent?

ANSWER. The pre-CICA system allowed this by permitting DOD the discretion to limit competition to those contractors whose demonstrable technical expertise was far superior to other prospective offerors. By severely restricting sole source and limited competition, the Services are compelled to de-emphasize quality to enable questionable offerors a chance to compete.

You cannot magically redefine quality to ensure its existence. DOD must be given the authority to seek it out and the incentives to settle for nothing less.

Senator DIXON. On the specific issue of warranties, concerns have been expressed that warranties are being required without regard to technical risk or cost. During our October 17 hearings with Dr. Wade, we raised the issue of cost/benefit analysis and the use of the statutory waiver authority.

How do you view the fact that only minimal use is being made of the authority to waive warranty requirements on defense contracts?

ANSWER. The fact that only one waiver of the warranty mandate has been sought should provide Congress with a big, obvious warning that cost effectiveness determinations are not being made realistically. A great disincentive to reaching good cost benefit analyses is in the Congressional reporting requirement. How many DOD program managers want to buy a trip to Capitol Hill for themselves and their bosses with a truthful finding that a performance warranty is not cost effective?

Senator DIXON. Has it been the experience of your member companies that the services are conducting thorough cost/benefit analyses in weighing their decision of whether to require a warranty for a given product?

ANSWER. Our experience is limited and anecdotal. We have found that DOD is generally assuming that warranties pass the cost/benefit test.

Senator DIXON. One of the concerns I have heard expressed is that each of the services are "going their own way on warranty policy."

In your view, what are some of the inconsistencies in the manner in which the services have implemented the warranty legislation?

ANSWER. These inconsistencies range from making the warranty an element of competition to requiring a warranty before a system is in mature full-scale production. Making the warranty an element of competition presupposes cost-effectiveness by requiring an offeror to include the cost of the warranty in his price. No identification of separate warranty costs is permitted in many cases.

QUESTIONS SUBMITTED BY SENATOR JOHN GLENN

Senator GLENN. During the past two weeks we have heard several witnesses from DOD, including Dr. Wade, testify that there have been serious problems implementing the 1984 legislation and that Congress should resist further procurement reform legislation until they have had time to fully assess the impact of the 1984 legislation.

Now, I see several of you from industry are recommending the same thing.

Since this course of action is not realistic and given the scope of the proposed 1985 procurement reform legislation, can you give us your views on what impact the passage of all or most of the 1985 legislation will have on the efficiency of the DOD acquisition system?

Answer. The principal effect of the 1985 legislation is likely to be the same as the 1984 legislation—additional red tape which lengthens procurement lead times and increases costs. The new emphasis on expanding the power of auditors, at the expense of contracting officers' authority, creates a conflict between the two. The contractor, now more than ever, will have difficulty in telling who is the boss.

Auditors, engineers, and lawyers are employed in the corporate world to give the businessman advice, not to make decisions for him. If you want to increase the efficiency of defense procurement, try to increase the ability of the contracting officer to act like a businessman and not a functionary of those who should only be advising him.

Senator **Glenn.** Dr. Wade testified that quality was on the top of his agenda for the future. He stated that in DOD acquisition, competition is too frequently based on price and an "award to the low bidder" mentality is too extensive.

Dr. Wade indicated that DOD plans to move away from defining equipment requirements in minimally acceptable terms to a system whereby the best quality equipment at an acceptable price is their recognized objective.

My observations have been that there has been too much emphasis on cost at the expense of quality. I would appreciate your comments on cost versus quality as related to current procurement regulations.

Answer. Dr. Wade's emphasis on quality is entirely appropriate. New statutory requirements may well make his goals unachievable.

The emphasis on cost reduction and competition is appropriate. But when it is taken to extremes, as it has been recently, quality suffers.

Consider the example of the legislation which requires the surrender of rights in technical data as an element of competition. Section 201 of Public Law 98-577 does just this.

This provision tells a prospective contractor that he will have to surrender his competitive advantage to secure a contract. By giving up his rights, he may also prejudice his competitive position on other projects which could benefit from the same research and development which provided the advantage on the first contract. This simply de-emphasizes quality and technological advancement by making the offeror limit, to the greatest extent he can, the amount of technical data used in any offer. Contractors should be given incentives to keep their advantages so that they can always offer the most advanced technology in every offer.

Senator **Glenn.** We have heard testimony that dual sourcing is an excellent technique for reducing program risk and production costs in selected situations, but it is not the panacea that current legislative proposals would lead one to believe.

I also read recently where the Navy has issued an order directing that all new weapons programs will have two sources.

I would appreciate your comments on the value of dual sourcing, both the leader-leader approach and the leader-follower approach.

Answer. Dual sourcing only makes sense where there is sufficient work to enable both contractors to recover their investment. Without this assurance, each contractor's price will be higher than necessary to assure a profit on high-investment, low-volume work.

SECNAV Instruction 4210 is a good example of what should not be done to assure dual sourcing. This new Instruction, issued on November 20, mandates the dual sourcing of full-scale engineering development contracts. It provides that the Navy will not pay for special tooling and equipment. Last, and most importantly, it recognizes the mandate of CICA and thus tells each contractor that while he is expected to tool up for 100% of the work, the risk is all his in a winner-take-all production award. This is precisely the approach which will cause cost overruns and decrease quality by requiring contractors to take inappropriate levels of risk without assurance of recovery of their investments.

Senator **Glenn.** There has been concern expressed that procurement reforms have curbed the flexibility and authority of program managers. It has been suggested that several pilot programs be identified where most regulations could be waived and managers given a free hand.

The goal would be to see what managers can do if instructed to "use good management and common sense."

Do you believe this would be a worthwhile project?

Answer. This is the best idea to come along since the flood of procurement reform started over two years ago. Many people refer to the Secret (i.e., "black") programs as models of efficiency. In comparison to regular procurement, they are because they are free of the endless reviews and cross-checks which burden other programs.

Congress should quickly authorize several test programs and, in doing so, make it clear that a free hand is really being given. Authorize the programs and then ignore them until they are completed. Don't burden them with the reporting requirements which multiply with each new law. Also, make it clear that quality is the goal, not multiple sourcing, warranties, surrender of patent and data rights and the like.

If real incentives to efficiency and quality are provided Congress will be surprised at how good a system it will get and at what will prove to be a reasonable cost.

CONCLUSION

I hope you will find these answers of assistance to you in your oversight and legislative tasks. EIA and I stand ready to assist you in any further investigation of recent changes in the law.

Sincerely,

JOHN D. RITTENHOUSE.

[Enclosure.]

ELECTRONIC INDUSTRIES ASSOCIATION,
Washington, DC, December 12, 1985.

Hon. DAN QUAYLE,
Chairman, Subcommittee on Acquisition Policy, Committee on Armed Services, U.S. Senate, Washington, DC.

DEAR MR. CHAIRMAN: On behalf of the Association, I want to thank you for providing us and Mr. John Rittenhouse the opportunity to present our views during your November 7 hearings regarding the effects of recent legislative reforms on the DOD procurement system. We support your subcommittee's ongoing effort to monitor implementation of statutory changes to the Defense acquisition process and policies. We would further solicit your active and continuing involvement to ensure that DOD's regulatory implementation reflects the intent of the law.

We are pleased to provide you with these additional views concerning problem areas in which we believe current statutory or regulatory requirements are having counter-productive effects on the procurement system. We wish to recognize, however, that too little time has passed in which to evaluate the full effects of reform legislation passed to date. Over time, we would propose to offer additional insights on the effects of much of this legislation as the DOD acts to implement it. To this end, we solicit your assistance in maintaining a continuing dialogue on issues surrounding procurement reform.

Many of the procurement reforms enacted over the past two years seem to be aimed at achieving perfection in defense procurement. They do so by imposing additional controls on the contractor and the government contracting officials with whom we deal. But a flawless system has not been and cannot be devised. Thus, these reforms serve mainly to expand the powers of inspectors, auditors and the other "checkers" at the expense of the contracting officer.

No businessman hires an auditor, a lawyer, or an engineer for the purpose of surrendering his business decisions to him. Commercial businesses conduct themselves efficiently because the decision makers can seek advice from experts but are free to discount their advice if it makes good business sense to do so and if they are not otherwise restrained by law.

There are strong reasons for defense procurement to emulate the commercial system. We offer this as a theory to guide your evaluation of the laws recently enacted and your formulation of future legislation: give the contracting officer the responsibilities and the authority to carry them out. To increase the effectiveness of defense procurement policies, put them in the hands of the action officer. Increase his ability to act like a responsible businessman and not as a mere conduit for the decisions of those who should be advising him.

Our specific comments will be divided into three categories of concern: 1) Legislative provisions currently in force which require modification or outright repeal; 2) Instances of regulatory implementation which represent substantial over-reach of legislative intent; and 3) Areas in which the military services have pursued major, independent forays into procurement reform.

1. LEGISLATIVE REPEAL MODIFICATION PROPOSALS

These suggestions will be divided into two categories, those enacted (a) prior to CY 1985, and (b) those enacted during CY 1985.

Diminution of contracting officers' authority

In drafting recent legislation, Congress has failed to distinguish clearly between its mandates and its suggestions. For example, in the case of DOD's authority to waive the warranty requirements, Congress provided wide discretion to waive the provision for lack of cost-effectiveness but mandated the reporting of each waiver to both Armed Services Committees.

In cases such as these DOD is left with no discretion at all. When every decision is questioned by one congressional committee or another procurement decisions will always be made on the safest political basis. The most stringent interpretations will be placed on every limitation whether Congress intended that it be so or not. For that reason, Congress must indicate its mandates more clearly and leave its suggestions out of the law. Burdening decisions with reporting requirements such as those imposed by the warranty statute predetermines how those decisions will be made.

Warranties

(See also Regulatory Overreach below.)

The fact that only one waiver of the warranty mandate has been sought should provide Congress with a big, obvious, warning that cost effectiveness determinations are not being made realistically. A great disincentive to reaching good cost benefit analyses is in the congressional reporting requirement. How many DOD program managers want to subject themselves and their supervisors to a trip to Capitol Hill to report a truthful finding that a performance warranty is not cost effective?

We would urge that this reporting requirement be repealed, and that the Office of the Secretary of Defense be delegated the responsibility for oversight of performance warranty waiver requests.

Commercial pricing of supplies

(See also Regulatory Overreach below.)

PL's 98-525 and 98-577 require contractors to certify that the prices of commercial items that they offer to the government are as low as or lower than the lowest prices offered to their best commercial customer or, to identify the reason for the higher price (with exceptions granted for differences in quantity, quality etc). The laws differ slightly in that PL 98-577 (for civilian agencies) specifies application to "Spare Parts" and 98-525 (for the DOD) does not. It would ease implementation of this statutory provision to have the legislated language in 98-525 changed from the all-inclusive term "supplies" to "spare parts". This is in conformance with the legislative intent as noted in the conference report language.

Rights in data

(See also Regulatory Overreach below.)

The Congress specified in PL 98-577 that the government should obtain rights to data. The language strongly suggests limiting a contractor's rights in data to a period of seven years as a negotiation objective. The language is sufficiently stringent that it essentially mandates using seven years as an unnegotiable maximum and suggesting that a lesser time in desirable. In fact, recent experience seems to indicate a general tendency of the DOD to obtain data in such short time frames even though the items being considered for procurement may warrant longer time periods. Furthermore, we fear that overemphasis on abrogation of contractor rights in data may stifle innovation in the government marketplace. Therefore, we suggest elimination of language specifying a seven-year time frame for acquisition of rights in data.

Lowering threshold requirement for certified and pricing data submission to $100,000

In enacting the Deficit Reduction Act of FY '85, Congress acted to lower the threshold for providing of cost and pricing date from $500,000 to $100,000. This lower threshold results in greatly increased paperwork and related costs of contract administration, and is particularly burdensome to smaller businesses acting as prime and sub-contractors. The DOD noted in mid-1983 that a $500,000 threshold lessens DOD contract administration costs by almost 80%, while maintaining certification requirements for over 90% of Defense dollars. Even if the ceiling is returned to the higher level, contracting officers retain the right to obtain cost and pricing data whenever they believe it is necessary. Therefore, the lower threshold is unnecessary, counterproductive, and should be raised to $500,000.

Additional suggestions for statutory modification/repeal of provisions passed during CY 1985 include:

Work measurement/"standard work hours" requirements

While we support the thrust of Senator Levin's introduction of S. 1783, which seeks to delay implementation of the Boxer/Grassley amendment to the FY '86 Authorization Act to permit hearings by the Senate on these experimental provisions, we continue to urge that the "standard work hours" legislative requirements should be repealed. Our membership would urge repeal in recognition of the inherent differences in the defense manufacturing environment versus its commercial industry counterparts. Defense specifications and small, batch-type production runs common to Defense manufacturing make the process of developing commercial-style work standards a complicated process of dubious practical value, at best.

In addition, we have the following clarifying amendments to offer toward an improved version of S. 1783:

Change the words "defense agency" in line 1 and 2 at the top of page 2 to read "contractor".

Reason.—It has always been a matter of whether the contractor keeps the records, not the agency. This appears to be a drafting error.

Change "180" days on line 10 page 2 to "360" days.

Reason.—180 days may not provide sufficient time for hearings on this very complex subject. The DOD authorization bill which this bill is amending was signed into law on Nov. 8, 1985 (P.L. 99-145) which means the 180 days would end on May 8th, 1986.

Change the words "the date of enactment of such section" on lines 17 and 18 to read "the effective date under 2(a) above."

Reason.—The existing language would make this requirement effective on Nov. 8, 1985, the date the DOD authorization bill was signed, when the objective of S. 1783 is to delay the effective to permit hearings on the subject.

Change the word "before" on line 20 of page 2 to "after".

Reason.—This requirement should not be made applicable to existing contracts.

Delete the words "if such contracts have not been completed or otherwise terminated before such date" on lines 20 and 21 at the bottom of page 2

Reason.—Same as above. Should not be made applicable to existing contracts.

Shift to contractor of burden of proof for cost reasonableness

This provision in the FY '86 Authorization Act overturns longstanding legal precedent of the *Bruce Construction* case. Under *Bruce Construction* costs incurred by a contractor are legally presumed to be reasonable. One cornerstone of contract law has been that government contractors, being prudent businessmen in a competitive market, would spend no more than necessary to do the job in order to preserve their competitive standing. By reversing this case, Congress has deprived the courts and administrative Boards of their test for reasonableness.

Disallowance of contractor costs incurred in State level lobbying activities

One little-heralded alteration of cost allowability policy in the FY '86 Defense Authorization Bill, was a provision barring allowability of costs incurred by contractors for state-level lobbying activities. This created an inequity in the government's approach to state level lobbying, since non-profits and government grantees' costs were not similarly made disallowable by the Act. We have long maintained that many state-level lobbying activities are carried out in direct furtherance of contracts being performed at locations around the country, and that such activities should be allowable to the extent that they directly benefit performance under DOD contracts. Examples of such activities would include lobbying to promote zoning changes, road and highway construction, etc. At a minimum, contractors should be afforded commonality of treatment vis-a-vis non-profit organizations in decisions on allowability of these costs.

Implementation/effectiveness dates

The magnitude of the legislation enacted in 1985 overloaded DOD's regulatory system to such an extent it resorted to interim regulations which in some cases went beyond the intent of the legislation, and has and is taking much time and money on the part of industry and the government to resolve. Many of the implementation problems being experienced, e.g., DOD's use of interim regulations without the benefit of public comment by industry can be laid on Congress' doorstep. Instead of specifying in the legislation the effective dates for implementation in terms of a specified number of days after enactment, a more appropriate and less confusing way would be to specify implementation in terms of proposed regulations to be issued in so many days, with a minimum public comment period of 60 days provided before final regulations are made effective.

An alternative would be to specify in the statutes when establishing implementation dates that a minimum of 60 days for public comment shall be provided.

2. REGULATORY OVERREACH IN IMPLEMENTATION OF RECENT LEGISLATION

A major industry concern arising from recent legislation and regulatory initiatives is the lack of regulatory uniformity among the various procuring departments and agencies. In enacting the Uniform Federal Procurement System, Congress clearly intended that a high degree of uniformity should exist in the rules under which the government procures needed goods and services. Government agencies were given authority to implement and supplement acquisition regulations, but not to incorporate conflicting or duplicative coverage into their supplements. Multi-agency coordination and centralized sanction to deviate from established policy are also standard procedural requirements.

Regulatory over-reach has been a particular problem in three major issue areas discussed below:

Warranties

The first concern, underlying an inequity in the statute, is that it imposes product and specification performance warranty liability on the contractor even though the designs and specifications are the government's or are under government control. The statute's legislative history (Senate Report 98-500; House Report 98-1080) states, inter alia, that performance guarantees could be narrowed in cases where the contractor has not had sufficient control over design and development that it could fairly be asserted that performance deficiencies would be the contractor's fault. In practice, this legislative intent has been ignored. The defense agencies have insisted on obtaining contractor performance warranties, indiscriminately, without regard to this legislative concern.

Compounding the excessive performance warranty demands, defense agencies often disclaim any responsibility for the suitability of government-furnished specifications, designs and drawings. Through such practices, the warranty statute is becoming an inducement to the government to become careless in satisfying its responsibility to furnish the contractor an adequate baseline for preparing bids. Inevitably, the government's failure to stand behind its designs and drawings will reduce effective competition and cause increased prices.

A third problem relating to the statutory performance warranty relates to the policy of the defense agencies against the use of waivers. Implicit in the statute, and expressly emphasized in the legislative history is the thought that excessive performance warranty demands would be blocked by the requirement that each warranty requirement be justified on the basis of a cost-benefit analysis. Defense agencies, however, have announced policies of refusing to recognize any warranty cost in contractor's bids or of requiring contractors to submit contractual plans to assure no-cost performance warranties. Thus, by adopting the posture that warranties are being obtained from contractors at no additional cost, the defense agencies are negating the statutory safeguard.

Rights technical data

Section 1213 of the DOD Authorization Act for FY 1985 established the surrender of technical data as an element of competition. It enables DOD to demand the surrender of technical data, whether it is needed or not, as part of the price offered.

This approach burdens competition rather than aides it. By providing competition on surrender of data rights a company's position on pricing is seriously weakened. Its ability to include the price of development in its production item, as it must in any government or defense contract, is eliminated. Competition is healthy for the procurement system only if the competitors are permitted to recover their investments and strengthen their ability to continue developing technology which gives them and their systems a competitive advantage.

The Government for years has required that a contractor provide technical data and drawings relating to hardware being delivered under contract. Such data often includes trade secrets or other proprietary material which the originating contractor is unwilling to disclose, therefore, a contractor is permitted to limit the Government's "right to use" if the technical data is unpublished and pertains to an item, component or process developed at private expense.

The Defense Procurement Act and the Small Business and Federal Procurement Competition Enhancement Act of '84 mandated new Technical data regulations. The resultant regulations were published in the fall of 1985 and were subsequently withdrawn primarily due to objections raised by the industry as to the over-implementation of the statute. A more simplified version was then published as an interim rule pending final analysis and publication of a final rule expected sometime in early 1986.

Some examples of the executive overreach are as follows:

1. The rule required that a contractor provide unlimited rights in any technical data or computer software used by the contractor or any subcontractor or supplier at any stage of manufacture or development of the item being delivered under the contract.

2. The rule stated that a contractor's willingness to provide such data and rights may be evaluated as part of a source selection, whereas the Defense Authorization Act of '84 states that the contractor will not be required to provide technical data for commercial products or processes as a condition for obtaining a contract.

3. The rule permits the Government to order data at any level of detail within a product configuration that has been previously produced even though not currently under a contract.

4. The rule ignores an imperative of the "Defense Reform Act of '84" wherein, it is stated that regulations implementing the Act shall take into consideration how the technical data development was funded.

Since the final regulations have been withdrawn it is too early for industry to determine whether there is or will be a regulatory "over-reach" of the statutes. However, if the regulatory guidance issued by the Air Force and Navy since the legislation was enacted is indicative of what OSD eventually issues, the industry will once again face a serious statutory overreach on the part of DOD.

Commercial pricing of supplies

A final recent example of over-reach was Federal Acquisition Circular 84-10, in which a basically simple most favored commercial customer requirement was interpreted in such a way that a major, and virtually unnecessary recordkeeping burden was imposed upon government contractors. The authors of FAC 84-10 further compounded the problem by providing no opportunity for public comment prior to incorporating the circular into the FAR as an "interim" rule effective as of the date of publication.

3. INDEPENDENT UNAUTHORIZED PROCUREMENT POLICY REVISIONS OF THE MILITARY SERVICES

A third category of concern arises from the many recent initiatives by the individual Services without coordination and control by the designated acquisition management authorities of the Office of the Secretary of Defense.

Our members now see, on a routine basis, the independent generation of major procurement policy changes by elements other than the Office of the Secretary of Defense (OSD). Such independent approaches have recently been apparent in such diverse areas as: rights in technical data policies; travel costs reasonableness policy; requirements covering cost of contractor purchases of special tooling equipment; fixed-price contracting in full scale engineering development; and other areas. We urge the subcommittee to encourage the Office of the Secretary of Defense to reestablish its authority as the proper channel for establishment coordination and promulgation of defense regulations.

Finally, we urge the subcommittee to continue its oversight of DOD's implementation of recent legislation. In doing so, we trust the committee will ensure the uniform application of these initiatives throughout the procurement systems, and indicate its displeasure at regulatory actions which frustrate or over-reach Congressional intent.

In closing, we wish to offer the assistance of EIA representatives on an ongoing basis to assist the subcommittee in identifying issues in which additional Congressional involvement and oversight is needed. Again, many of the elements of reform legislation passed to date have yet to be implemented and evaluated by our industry. An ongoing dialogue with the subcommittee members and staff remains the best means of assuring the workability and cost-effectiveness of statutory and regulatory requirements.

Sincerely,

JEAN A. CAFFIAUX,
Senior Vice President, Government Division.

RESPONSES SUBMITTED BY MR. CHARLES W. STEWART, PRESIDENT, MACHINERY AND ALLIED PRODUCTS INSTITUTE, NOVEMBER 22, 1985

Hon. DAN QUAYLE,
Chairman, Subcommittee on Defense Acquisition Policy, Senate Armed Services Committee, Senate Russell Office Building, Washington, DC.

DEAR MR. CHAIRMAN: During the course of the hearing conducted on Thursday, November 7, the Subcommittee on Defense Acquisition Policy, you raised the questions concerning recently enacted defense procurement legislation. Specifically, you asked the members of the defense industry panel for recommendations as to statutory provisions which either should be repealed or revised. Having been represented on that panel, MAPI is responding to your request for what was referred to as a "wish list." Our recommendations deal principally with the four major defense procurement policy statutes which have been enacted into law since July 1984. We ask that this letter be included in the hearing record.

CERTAIN SPECIFIC SUGGESTIONS MADE BY MAPI DURING ITS TESTIMONY ON NOVEMBER 7

At the outset, we would like to repeat and/or amplify certain suggestions made to the Subcommittee on Defense Acquisition Policy in our written statement on November 7 as supplemented by oral testimony.

(1) When the Defense Appropriations bill goes to conference, we recommend strongly that the Senate block further procurement changes included in the House-passed bill.

(2) MAPI supports S. 1783 introduced by Senator Levin on October 22 which would amend Section 2406 of Title 10 of the United States Code—the so-called "work standards" provision. Indeed, it is the position of the Institute that the Congress should repeal Section 2406. Our letter of November 14 to Senator Levin in response to his request during the hearings on November 7 for industry comments on S. 1783 is attached as an appendix to this statement.

(3) The Congress should reexamine the legislative mandate to the Inspector General of the Department of Defense. The IG is truly a creature of the Congress and in reality functions independent of the Secretary of Defense and the DOD establishment. This, in our judgment, creates serious organizational problems and unnecessary conflicts. A study of the problem should be undertaken by the Congress and statutory amendments enacted in that light.

(4) We feel that it is incumbent on the Congress, and to some extent on the Department of Defense as well, to build a comprehensive record of defense industry technological accomplishments, which are extraordinary. Our principal statement on November 7 identified a number of such achievements.

(5) Through law and administration, a number of acquisition priorities have been developed and placed in effect. There are certain inherent conflicts between these priorities and, in our opinion, it is the obligation of the Congress and the procurement authorities to identify these conflicts and reconcile the priorities. We refer to such priorities as competition, quality, incentives for utilization of advanced technology in production, protection of proprietary rights, maintenance of an adequate industrial base, etc.

(6) We urge that Congress undertake a narrowing of the role of oversight and committee activity insofar as the procurement policy area is concerned. This, of course, will require a balancing of congressional deference and organizational discipline. There are entirely too many committees, subcommittees, staffs, and individuals in the act.

(7) The Congress should undertake an examination of the cost of regulation in the procurement area. In this measurement process, special attention should be given to the exploding cost of the audit function. And in examining cost, direct costs should, of course, be determined, but indirect costs impacting on the contracting process and the weapon production effort should also be examined. We refer to bogging down of defense production, diversion of contracting personnel—both government and industry—from such objectives as quality, etc.

(8) The Congress and the procurement authorities should undertake a joint investigation of the relationships between project managers, contracting officers, and auditors. It has become deliberate policy to give overriding authority to the auditing functions with the result that the project manager, and the contracting officer in particular, are relegated to lesser roles and deprived of certain incentives which are necessary to achieve the best results.

(9) The Congress should also examine into what appears to be the development of certain autonomous procurement postures and actions by individual services. Is the Department of Defense at the OSD level really in charge?

COMPETITION IN CONTRACTING ACT (PUBLIC LAW 98-369, JULY 18, 1984)

Overemphasis on competition

Section 2723 of the Act revises Section 2304 of Title 10 of the U.S. Code to require the government generally to obtain "full and open competition through the use of competitive procedures . . ." in procuring property. Paragraph (c) of Section 2304 limits the use of other-than-competitive procedures to seven specified instances.

In our view, the application of these provisions to the acquisition of major weapon systems may cause very serious problems. For example, following the development of a system, if there is to be a production contract calling for the delivery of very few units of that system, is the establishment of an alternative source of supply at that stage required by the Act? Paragraph (d)(1)(B) of Section 2304 would permit the use of other-than-competitive procedures in the case of such a follow-on contract when an award to an alternative source would result in "substantial duplication of cost to the United States." Beyond cost to the government, the cost to the original source might be very substantial, cause severe economic problems for that original source, and endanger its availability to the government in the future.

In brief, we think that the statutory emphasis on competition, together with the overly narrow language of the exception for noncompetitive follow-on production contracts, has the potential to cause counterproductive costs to the government and severe economic problems for those companies which are the primary developers of new weapon technology. Consequently, we urge that these statutory revisions be reconsidered in this light.

Burdensome paperwork and recordkeeping requirements

Paragraph (f) of the revised 10 U.S.C. 2304 includes new requirements with regard to justifications and approvals when other-than-competitive procedures are used. In the case of a contract exceeding $10 million, such approval must be made by the senior procurement executive of the agency, and a detailed statement of justification must be furnished in that connection.

We think that these new requirements are likely to be quite burdensome, and we urge the Subcommittee, as a matter of priority, to review initial government and contractor experience with these requirements and consider possible legislative changes.

The role of the competition advocates

Section 2732 of the Act adds a new Section 20 to the Office of Federal Procurement Policy Act, which establishes a competition advocate for each executive agency who, under paragraph (b) of that Section, is given detailed responsibilities with respect to reviewing and commenting on individual agency procurement actions.

In our view, the role of the competition advocate is far too open-ended. The basic responsibility of the competition advocate seems to be to assure that competition is attained as a matter of top priority in any individual case. This is likely to cause problems for a contracting officer who—we think properly—may view the obtaining of reasonable prices and achievement of high quality, rather than maximization of competition, as the primary objective in negotiating an individual contract. The problem of the open-ended role of the competition advocate and the relationship between the competition advocate and the contracting officer, may be compounded by Section 1216 of the Defense Procurement Reform Act which requires that each agency competition advocate shall be a general or flag officer or, if a civilian, a grade GS-16 or higher. The difficulty that this may cause for a medium-grade civilian contracting officer is clearly foreseeable.

DEFENSE PROCUREMENT REFORM ACT OF 1984 (TITLE XII OF THE FISCAL YEAR 1985 DEFENSE AUTHORIZATION ACT, PUBLIC LAW 98-525, OCTOBER 19, 1984)

Cap on contractor proprietary rights in technical data

Section 1216 of the Act adds a new section 2320 to Title 10 the U.S. Code Paragraph (c) of that Section states that the statutory provisions should not be construed to prohibit the Secretary of Defense from prescribing standards relating to contract provisions for "caps" on contractor limited rights (proprietary) technical data. Specifically, such contract provisions, under paragraph (c), could provide for a specified period of time, not to exceed seven years, after which the United States would have the right to use, for any purpose, data which it orignially had acquired from a contractor subject to limitations concerning the government's right to use such data.

Our problem with this provision is that it gives the Department of Defense (DOD) what appears to be a carte blanche authority to develop such regulations, without any indication as to the policy criteria which should be considered by DOD in drafting such regulations. This issue is obviously of considerable importance since both the Air Force and the Navy have already established their own policies on this issue prior to the promulgation of any overall DOD policy.

As a general proposition the Subcommittee should maintain close oversight as to technical data since this is a critical area for contractors and subcontractors with proprietary rights.

Commercial pricing certification requirement

New section 2323 of Title 10, also added by Section 1216 of the Act, establishes a requirement that a contractor shall certify in an offer for the sale of items that the price offered is not more than its lowest commercial price for the items, or shall submit with the offer a statement specifying the amount of the difference and providing a justification for that difference.

As we have indicated in our testimony on November 7 to the Subcommittee, we think that there are a number of difficulties with the statutory language which, in turn, have led to substantial problems in trying to formulate appropriate implementation of these provisions in the Federal Acquisition Regulations (FAR). Specifically, we think that the statutory provisions should be reviewed and considered for amendment with the following points in mind:

(1) The original House and Senate bills referred to application of such a certification requirement to contractors for the procurement of replenishment and spare parts, not to contractors for the procurement of items generally.

(2) There should be an express exclusion from the certification requirement for sales to original equipment manufacturers (OEMs) and dealers who add either product or marketing value and resell to end user customers.

(3) There should be a de minimis figure on sales to nongovernment parties that must be taken into consideration in determining whether the government has been offered the lowest commercial price for the item in question.

Contractor guarantees

Section 1234 of the Act adds a new Section 2403 to Title 10 of the U.S. Code requiring contractor guarantees in connection with the procurement of major weapon systems. There are two major issues with this provision which, in our view, warrant consideration by the Congress.

The first concerns the requirement that the contractor guarantee that the item "will conform to the essential performance requirements of the item as specifically delineated in the production contract." We feel that this requirement should not be included in the guarantee provision. The following two guarantees should be sufficient: (1) the item will conform to the design and manufacturing requirements specifically delineated in the contract, and (2) the item, at the time of delivery, will be free from all defects in materials and workmanship. Another problem with the "essential performance requirements" guarantee is that there may well be instances where the contractor does not fully understand or appreciate what constitute the essential performance requirements as distinguished from the design and manufacturing requirements with respect to the item.

The other major issue as to guarantees relates to paragraph (d) of the provision which authorizes the Secretary of Defense to waive the guarantee requirements when he, or his designee, determines that a guarantee would not be cost effective. It is our understanding that this authority has been used in only one instance; clearly this is an "underuse" of the waiver authority which we think is not in accordance with the intent of Congress. Under these circumstances, we think that consideration should be given to revising the statutory language to indicate more clearly Congress' intent with respect to this matter. The Congress should encourage the use of the waiver authority when appropriate.

SMALL BUSINESS AND FEDERAL PROCUREMENT COMPETITION ENHANCEMENT ACT OF 1984 (PUBLIC LAW 98-577, OCTOBER 30, 1984)

Section 302 of the Act adds a new Section 22 to the Office of Federal Procurement Policy Act which specifies that no procurement policy, regulation, procedure, or form shall take effect until 30 days after it is published for public comment in the Federal Register, and that interested parties shall be afforded no less than 30 days to provide such comments, Paragraph (d) of the provision permits a waiver of these requirements, if "urgent and compelling circumstances make compliance with such requirements impracticable."

DOD used the exception to put the new overhead cost certification requirement into effect last March without prior public comment. Subsequently, DOD together with NASA and GSA, used the exception with respect to the commercial pricing certification requirement and other provisions included in FAC 84-10 and FAC 84-11. To date, the exception has been used so often that it is close to becoming the general rule. At the minimum, what needs to be done is to make clear to DOD that the exception proviso should be used only in a limited manner and that, when used, the "urgent and compelling circumstances" should be spelled out. Otherwise the "opportunity to comment" provision becomes a sham.

DEFENSE PROCUREMENT IMPROVEMENT ACT OF 1985 (TITLE IX OF THE FISCAL YEAR 1986 DEFENSE AUTHORIZATION ACT, PUBLIC LAW 99-145, NOVEMBER 8, 1985)

Allowable costs under defense contracts

Section 911 adds a new Section 2324 to Title 10 of the U.S. Code, concerning allowable costs. Paragraph (e)(1) lists ten specific cost items as unallowable, although the Secretary is given authority to establish, by regulations, appropriate definitions, exclusions, limitations, and qualifications.

We understand the motivation for this legislation, as indicated by the report of the House Armed Services Committee on the proposed "Allowable Cost Reform Act" (Section 2 of that bill is the origin of the new Section 2324).[1] In brief, the Committee referred to its intent to "remove any doubt as to [the] allowability [of the costs identified] and to state as a matter of Congressional policy that such costs will not be chargeable to Department of Defense contracts."

On the other hand, it seems clear from experience in this area that it is not desirable to attempt by legislation to spell out detailed rules concerning cost allowability. For example, the second item listed is "costs incurred to influence (directly or indirectly) legislative action on any matter pending before Congress or a State legislature." There experience of the Executive branch of the government with regard to OMB Circular A-122 and problems resulting from the effort to establish lobbying cost allowability limitation rules for all government agencies, indicate the compelling need for flexibility in determining cost-limitation rules respecting legislative activities. Are the same rules to be applicable to communications to a member of Congress, to a congressional staff member, and to an appearance to present testimony before a congressional committee at a public hearing? Clearly the statutory language should be reexamined to provide more flexibility.

We think that similar issues arise concerning other cost items, and they indicate the desirability of proceeding through administrative regulation rather than legislation, in establishing cost-limitation rules. A congressional reexamination is urged.

Post-Government service employment bars on senior officials

Section 921 of the Act imposes a two-year bar on the employment of a Presidential appointee by a defense contractor when that person has acted as a primary government representative in the negotiation of a government contract with that contractor.

We, of course, are aware of the extensive controversy concerning this provision and the suggestions from certain members of Congress, particularly in the House, that the two-year bar be extended broadly across the board to cover all DOD employees, both military and civilian, above a certain grade or salary level. Nevertheless, we continue to feel that *any* such employment bar is unwise as a matter of public policy. It seems evident that the bar established by section 921 on Presidential appointees, to the extent that it covers civilian officials, will act as a substantial disincentive to potential candidates from accepting high-level DOD positions, when they know that, as a consequence, they may be barred for a two-year period from certain positions in defense industry.

Penalties concerning contractor submission of cost and pricing data

Section 934 of the Act provides for certain penalties for contractor submission of inaccurate, incomplete, or noncurrent cost and pricing data if the submission of such data "was a knowing submission." This provision raises what seems to us a very serious question. The adjective "knowing" appears to modify "submission" rather than "inaccurate, incomplete, or noncurrent cost and pricing data." That being the case, the penalty presumably will apply if the submission of cost and pricing data by the contractor is a knowing act on its part, even though there was no knowledge on the part of that contractor that the data in question was inaccurate, incomplete, or noncurrent. The statutory language should be reexamined and, we believe, clarified.

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[1] House Report 99-169, 99th Congress, 1st session, page 11.

MAPI is pleased to submit these further recommendations with respect to recent defense procurement policy legislation. If we can be of assistance in other ways, please do not hesitate to call on us.

Sincerely,

CHARLES STEWART, President.

APPENDIX

MACHINERY AND ALLIED PRODUCTS INSTITUTE,
Washington, DC, November 14, 1985.

Hon. CARL M. LEVIN,
U.S. Senate, Senate Russell Office Building, Constitution Avenue, NE., Washington, DC.

DEAR SENATOR LEVIN: During the course of the hearing conducted on Thursday, November 7, by the Senate Armed Services Subcommittee on Defense Acquisition Policy, you requested the views of the members of the defense industry panel on your bill S. 1783. As one of the members of that panel, I am responding to your request.

S. 1783, which you introduced on October 22, would amend Section 2406 of Title 10 of the United States Code (an entirely new provision added by Section 917 of Public Law 99-145, the Fiscal Year 1986 Defense Authorization Act). Section 2406, which has generally been referred to as a "work standards" provision, requires defense agencies to "cause to be recorded" a considerable amount of contractor data, including (1) proposed and negotiated cost and pricing data, (2) proposed and negotiated bills of labor, (3) proposed and negotiated bills of material, and (4) incurred costs.

In brief, your bill, S. 1783, would delay the effective date of Section 2406 to 180 days after the enactment of the Defense Authorization Act, which would be May 7, 1986. In addition, in a related provision in the bill, the requirements in Section 2406 for a defense agency to record, in connection with any covered contract, information required under that provision, would be made specifically inapplicable if the contractor does not maintain such information on that section's effective date.

We strongly endorse your bill's provision for a six-month delay in the effective date for Section 2406. As you know, Section 2406 was added to the Defense Authorization Act as a result of an amendment by Senator Grassley, adopted on the Senate floor on May 24. Despite the opposition of the Defense Department and the fact that no hearings on the proposal had been held by the Armed Services Committees in either House of Congress, a virtually indentical provision, sponsored by Congresswoman Boxer, was approved on the House floor on June 26. We concur in the comments you made when you introduced S. 1783:

* * * The information gathering and reporting requirements under the current section will be expensive to implement by the Government because of both the increased costs associated with the contractual modifications that will be required and because of the additional internal Department of Defense systems that will need to be established. It will also cost a great deal to the companies who do not already collect this information. We should not randomly require expensive new recordkeeping and reporting requirements where the value of this information to Congress and to Pentagon auditors, analysts, and negotiators is so questioned and unclear."

Moreover, we are pleased to note that H.R. 3606 (identical to S. 1783) was passed by the House on October 28.

Finally, with respect to the underlying issue, the merits of Section 2406, we strongly urge that the Congress move promptly to repeal—or, at the minimum, to substantially revise—Section 2406. As you know, the Senate Judiciary Subcommittee on Administrative Practice and Procedure, chaired by Senator Grassley, held a hearing on July 25 on the general subject of work standards. During the course of that hearing, what we believe to be a very persuasive statement against Section 2406 was made by the then-Deputy Under Secretary of Defense for Acquisition Management. To quote briefly from her testimony:

"In [the] judgment [of the Office of the Secretary of Defense], many provisions of the legislation are ambiguous and subject to mininterpretation. There is uncertainty as to the types of contracts to which it applies. The legislation does not clearly identify the type of labor which it is presumably intended to track—i.e., direct manufacturing labor. There are questions as to amount and type of data to be recorded and reported and subcontractor applicability. To the extent clarification in these areas can be provided in the conference report or during these hearings, DOD implementation will be greatly facilitated. We in the DOD recognize, however, that intent is sometimes different that the language of legislation—and that, in the case of any conflicts, the language of the legislation is the controlling factor.

"It is our perception, perhaps incorrect, that the legislation is predicated on the beliefs that the data requested is readily available, easily summarized, always nonproprietary in nature, easily understood and interpreted, and is being withheld by DOD officials. These are simply not the facts."

If you have any questions concerning our views on S. 1783 or Section 2406 or if we can otherwise be of assistance, please let us know. Meanwhile, MAPI wishes to express its appreciation for the opportunity to testify on November 7. The activities of the Subcommittee represent a vital and constructive effort.

Respectfully,

CHARLES STEWART, *President.*

QUESTIONS SUBMITTED BY SENATOR ALAN DIXON

GENERAL

Senator DIXON. On October 29, the Joint Logistics Commanders testified before our Subcommittee. I would like to put one of the same questions to you that we asked of them.

Which acquisition legislation currently in effect would you like to see modified or repealed?

Mr. STEWART. This question is answered in detail in our letter of November 22, 1985 to the Subcommittee.

REGULATORY PROCESS

Senator DIXON. Gentlemen, you each devote a large proportion of your statement to concerns about the manner in which the Department of Defense has implemented the 1984 defense procurement legislation.

To what extent have the difficulties that you describe resulted from lack of clarity in the original legislation in such areas as definitions, scope of coverage, et cetera?

Mr. STEWART. In general, we feel that most of the difficulties with recent procurement legislation have resulted from too much specificity and detail in that legislation, which has led in many instances to what we regard as congressional over-management or micro-management of the procurement process. On the other hand, there are a number of instances in which a lack of clarity or specificity has created problems. Our letter to the Subcommittee on November 22, 1985 discusses some of these instances:

(1) The overemphasis on competition in Section 2723 of the Competition in Contracting Act;

(2) The lack of criteria for determining the time limits on "limited rights" on contractor technical data in Section 1216 of the Defense Procurement Reform Act;

(3) The lack of criteria for exercise of the guarantee requirement waiver in Section 1234 of the Defense Procurement Reform Act; and

(4) The lack of criteria concerning DOD's exercise of the "urgent and compelling circumstances" exception to the regulatory rulemaking requirements of Section 302 of the Small Business and Federal Procurement Competition Enhancement Act.

In addition, in our view, serious implementation problems have been caused by delays on the part of the Defense Department in getting regulations issued and its general unwillingness to issue these regulations first in proposed form as is required by Section 302 of the Small Business and Federal Procurement Competition Enhancement Act. Both of these factors may have resulted from DOD simply having too much legislation to implement at the present time.

Senator DIXON. What specific actions do you recommend that we take to introduce additional clarity into the legislation enacted over the past 2 years?

Mr. STEWART. As we have already noted, our November 22, 1985 letter to the subcommittee discusses in detail our recommendations concerning recent procurement legislation. We recommend that, as a general proposition, when Congress delegates authority to the Defense Department to promulgate regulations, issue waivers, avail itself of exceptions to otherwise applicable requirements, and the like, Congress provide at least general criteria relating to the exercise of such authority.

With respect to future proposed procurement legislation, we recommend that the Armed Services Committee try to establish a precedent that such proposed provisions not be adopted by the Senate until and unless first approved by the committee following public hearings on the specific provisions being proposed.

Senator DIXON. One strong general feeling that I get from all the witnesses is that there is not adequate and timely dialogue between the Department of Defense and the defense industry in the implementation process.

What steps can be taken to involve the industry and other affected parties at the front end of the rule-making process without adversely affecting the need for timely implementation of legislation.

Mr. STEWART. The Defense Acquisition Regulatory (DAR) Council must become more timely in its issuance of proposed regulations and more willing to discuss pending regulatory matters at an earlier stage than now seems to be the case. However, we recognize that these objectives may be difficult to accomplish in view of the substantial volume of recent legislation now awaiting implementation.

Secondly, Secretary Weinberger and Deputy Secretary Taft, both of whom have initiated new rules and regulations without resort to applicable rulemaking procedures, should be informed by the Congress that the rulemaking process prescribed by Section 302 of the Small Business and Federal Procurement Competition Enhancement Act must be utilized in the formulation of new procurement policy regulations. This might entail congressional action narrowing the availability of the "urgent and compelling circumstances" exception to the rulemaking requirements of Section 302.

QUALITY ISSUES

Senator DIXON. Every one of you have underscored the need to emphasize quality in selecting sources for defense products. There seems to be a general perception that competition is now being based predominantly on price considerations to the detriment of quality.

What specific actions should we consider to more properly balance concerns for cost and quality in defense acquisition?

Mr. STEWART. We have some concern that there is an overemphasis on competition in the Competition in Contracting Act. You may wish to consider appropriate amendments to that statute to stress the need for both quality and reasonableness in prices as well as for "full and open competition" as now required by the Act.

Senator DIXON. How should we define quality criteria so that the wisdom of making a contract award on the basis of quality rather than price is readily apparent?

Mr. STEWART. We believe that the statute should mandate DOD that, when quality should be the primary factor in a particular procurement, that fact should be acknowledged in the solicitation and in the proposal-evaluation process.

WARRANTIES

Senator DIXON. On the specific issue of warranties, concerns have been expressed that warranties are being required without regard to technical risk or cost. During our October 17 hearing with Dr. Wade, we raised the issue of cost/benefit analysis and the use of the statutory waiver authority.

How do you view the fact that only minimal use is being made of the authority to waive warranty requirements on defense contracts?

Mr. STEWART. We view with concern what clearly seems to be a minimal use of such waiver authority. DOD should be willing to use that waiver authority, without forcing one or more of the companies interested in the contract to risk losing the contract by requesting such a waiver. We think this problem should be correctable through appropriate congressional oversight which makes it clear that Congress expects reasonable—not minimal—use of the waiver authority. Beyond that, statutory amendments should be considered if they prove to be necessary.

Senator DIXON. Has it been the experience of your member companies that the services are conducting through cost/benefit analyses in weighing their decision of whether to require a warranty for a given product?

Mr. STEWART. We have no direct information on this but the fact that the waiver authority has been underused leads us to infer that through cost/benefit analyses have not been conducted in connection with determining warranty requirements.

Senator DIXON. One of the concerns I have heard expressed is that each of the services are "going their own way" on warranty policy.

In your view, what are some of the inconsistencies in the manner in which the services have implemented the warranty legislation?

Mr. STEWART. We have no information on this.

DATA RIGHTS

Senator **Dixon**. Mr. Stewart, you make the statement in your testimony that the new statutory provisions governing rights in technical matters "may be defective in certain respects" and you encourage our Subcommittee to reexamine it. You give one specific example in your statement, that of the "cap" on the length of time that data restrictions would apply.

What are other areas we should be monitoring?

Mr. **Stewart**. Among the areas we believe should be monitored are:

(1) The requirement in Section 1202(6) of the Defense Procurement Reform Act that persons who have developed products for sale to the public are not required, as a condition for selling that product to the Department of Defense, to provide the government with "unlimited rights" technical data relating to that product.

(2) The requirement in Section 2320(a) of the Defense Procurement Reform Act that technical data regulations are not to impair any rights established by law that a contractor may have in such technical data.

(3) The appropriate ". . . careful balancing of the need to acquire the rights in technical data for the purpose of enhancing competition while not stifling the initiative of American industry to develop leading edge technologies without government funding," referred to by Assistant Secretary Wade in his testimony to this Subcommittee on October 17, 1985.

Moreover, it is of critical importance that the effort to enhance competition by establishing alternative sources of supply, pursuant to new statutory requirements, does not (1) lead to driving original sources out of the defense industrial base by making it impossible for them to earn a reasonable profit on follow-on orders, and (2) cause a general degradation of quality with respect to items which have been alternatively sourced.

QUESTIONS SUBMITTED BY SENATOR JOHN GLENN

PROBLEMS IMPLEMENTING 1984 LEGISLATION

Senator **Glenn**. During the past 2 weeks we have heard several witnesses from DOD, including Dr. Wade, testify that there have been serious problems implementing the 1984 legislation and that Congress should resist further procurement reform legislation until they have had time to fully access the impact of the 1984 legislation.

Now, I see several of you from industry are recommending the same thing.

Since this course of action is not realistic, and given the scope of the proposed 1985 procurement reform legislation, can you give us your views on what impact the passage of all or most of the 1985 legislation will have on the efficiency of the DOD acquisition system?

Mr. **Stewart**. Almost certainly the 1985 legislation, at least in the short run (the next year or two), will be a drag on the efficiency of the acquisition system simply because of the need to promulgate new regulations despite the current backlog of unpublished regulations, and also because of the time that it will take for people both in government and industry to become accustomed to working with the new rules.

In addition, the efficiency of the acquisition system is currently being impaired by DOD over-regulation on its own initiative, and also by the growing cost of the control apparatus now in place.

Senator **Glenn**. Dr. Wade testified that quality was on the top of his agenda for the future. He stated that in DOD acquisition, competition is too frequently based on price and an "award to the low bidder" mentality is too expensive.

Dr. Wade indicated that DOD plans to move away from defining equipment requirements in minimally acceptable terms to a system whereby the best quality equipment at an acceptable price is their recognized objective.

My observations have been that there has been too much emphasis on cost at the expense of quality. I would appreciate your comments on cost versus quality as related to current procurement regulations.

Mr. **Stewart**. As we have indicated in response to Senator Dixon's question on the same point, we think that there is an overemphasis on competition in the Competition in Contracting Act. You may wish to consider appropriate amendments to that status to stress the need for both quality and reasonableness in prices as well as for "full and open competition" as now required by the Act.

Senator **GLENN**. We have heard testimony that dual sourcing is an excellent technique for reducing program risk and production costs in selected situations, but it is not the panacea that current legislative proposals would lead one to believe

I also read recently where the Navy has issued an order directing that all new weapons programs will have two sources.

I would appreciate your comments on the value of dual sourcing, both the leader-leader approach and the leader-follower approach.

Mr. **STEWART**. As indicated in our November 22, 1985 letter to the subcommittee, we have concern that dual sourcing may be overused. We believe that it may be entirely inappropriate in instances where it is not cost effective in the short run. There also may be instances in which its use, even though apparently cost-effective in the short run, may impose severe economic penalties on the original-source contractor, which may make it difficult for that contractor to remain in the defense industrial base and, thus, create substantial long-range problems.

Senator **GLENN**. There has been concern expressed that procurement reforms have curbed the flexibility and authority of program managers. It has been suggested that several pilot programs be identified where most regulations could be waived and managers given a free hand.

The goal would be to see what managers could do if instructed to "use good management and common sense."

Do you believe this would be a worthwhile project?

Mr. **STEWART**. Yes, we believe such pilot programs might well be worthwhile.

QUESTIONS SUBMITTED BY SENATOR ALAN DIXON TO MR. KARL G. HARR, JR., PRESIDENT, AEROSPACE INDUSTRIES ASSOCIATION OF AMERICA, INC.

Senator **DIXON**. On October 29, the Joint Logistics Commanders testified before our subcommittee. I would like to put one of the same questions to you that we asked of them.

Which acquisition legislation currently in effect would you like to see modified or repealed?

Mr. **HARR**. Senators Quayle and Levin also asked the same question at the conclusion of the hearings and I have responded separately in a letter to Senator Quayle. A copy of that letter to Senator Quayle follows:

AEROSPACE INDUSTRIES ASSOCIATION OF AMERICA, INC.,
Washington, DC, December 23, 1985.

Hon. DAN QUAYLE,
Chairman, Subcommittee on Defense Acquisition Policy, Committee on Armed Services, U.S. Senate, Russell Senate Office Building, Washington, DC.

DEAR MR. CHAIRMAN: At the conclusion of your Subcommittee's hearing on November 7, you and Senator Levin asked for specific suggestions as to statutory provisions which we believe should be either repealed or changed. The Aerospace Industries Association is pleased to offer several items for your consideration. Not all of these deal with specific areas of recently-enacted legislation. However, all are directly linked either to legislation or to the proliferation of regulations spawned by legislation.

As noted in my written statement, it is often not the precise language of a statute alone that presents a problem. Rather, the problems surface in the way the statute is interpreted and implemented through regulations. There is a trend toward over-regulation, going beyond what the statute required or what Congress intended. This spiral of one-upmanship results in excessive burdens on the entire contracting community, both industry and government. Not only does it inhibit the judgment and flexibility of contracting officials, but it adds to the complexity and volume of individual agency supplements to the Federal Acquisition Regulation (FAR).

Congress can help to reverse this trend, strengthen the process, and achieve greater uniformity in at least three important ways. First, Congress should not enact any more procurement legislation until the system has been able to digest the existing legislation and we can observe how it works. Second, Congress should limit the amount of legislation that applies to only one agency; in other words, needed legislation should generally apply across-the-board. Third, when it enacts procurement legislation that requires implementing regulations, Congress should require that such regulations be in the FAR and prohibit further implementation in agency supplements. A single, simplified, uniform procurement regulation, which is what the FAR was intended to be, is almost impossible to achieve under the present method of legislating procurement reform.

Reversing this trend and achieving greater uniformity will require discipline on the part of Congress as well as the Executive Branch agencies. The Legislative Reorganization Act of 1970 significantly increased the number of Congressional committees which have oversight authority over procurement legislation. Authorization and Appropriation bills are perennially late and, in addition, are used as vehicles to enact substantive legislation without adequate hearings or opportunity for discussion. We recommend a reduction in the number of committees and subcommittees having procurement jurisdiction. This, in itself, would facilitate greater discipline in the legislative process and minimize the possibility of conflicting, unnecessary, or ill-considered legislation, however well-intentioned.

A second area of much concern to industry is the changing role of the contracting officer, whose discretion and authority are greatly diminished by recent legislative and administrative changes. In almost every procuring activity, we find a proliferation of "advocates"—for competition, breakout, small business, specification control, small and disadvantaged business utilization—whose responsibilities overlap those of the contracting officer. The audit function has also become a dominant part of the negotiation process, further limiting the contracting officer's ability to exercise his or her judgment. Furthermore, the 1984 statutes require that the performance of contracting officers be evaluated on the basis of how well they have achieved goals for increased competition. Competition can and often does become an end in itself under such pressures, rather than a means to an end. Contracting officers should be evaluated on their business judgment and the quality of their performance, not on whether they have achieved some arbitrary goals. The trend toward Congressional micromanagement of the procurement process needs to be reversed to restore the concepts of responsibility and accountability to the role of the contracting officer.

In addition to the performance evaluation requirement contained in the Defense Procurement Reform Act of 1984, there are provisions in the FY 1986 Defense Authorization Act (P.L. 99-145) which further inhibit the contracting officer's business judgment. One of these deals with allowable costs, reflecting the misguided belief that determinations of allocability, allowability and reasonableness can be reduced to an exact science, doing away with any so-called "grey area". There is need for a better understanding of the role of price negotiations in contracting. One other provision, Section 933 of the Authorization Act, reverses the traditional "prudent businessman" test used in determining reasonableness of costs which are the subject of a contract dispute before either a Federal Court or the Armed Services Board of Contract Appeals. It places the burden of proof on the contractor to establish the reasonableness of such costs. This erosion of the long-standing "reasonable and prudent businessman" test is not only an unhealthy sign with respect to pricing of defense contracts, but also further diminishes the role and judgment of the contracting officer.

At this time, it is probably unrealistic to expect wholesale repeal of many of the provisions which contribute to the foregoing scenario. However, some specific legislative provisions which we believe should be repealed are as follows:

(1) Work measurement or "Cost and Price Management" as it is labeled in Section 917 of the FY 1986 Defense Authorization Act. We applaud Senator Levin's bill (S. 1783) which would delay the effective date of Section 917 for six months, but question whether even this is enough time in which to hold hearings and develop a better appreciation of the complexities of the subject. Without such an inquiry, any such legislation is premature at best. Therefore, Section 917 should be repealed until there is a demonstrated need.

(2) The Congressional reporting requirement in connection with waiver of warranty provisions contained in the Defense Procurement Reform Act (P.L. 98-525). The fact that only one waiver has been requested indicates that warranties are probably being required where they are not cost effective. The requirement to seek waiver approval from Congress is inhibiting. The responsibility for oversight of warranty waivers should be left to the Secretary of Defense.

(3) The requirements in Section 911 of the 1986 Defense Authorization Act that deal with the role of the auditor in connection with negotiation and settlement of contractor overhead. For example, the statute requires the auditor to be present at negotiations, that questioned costs be negotiated individually, and that the contracting officer shall not resolve any questioned costs until he has obtained the auditor's opinion. All of these requirements seriously inhibit the contracting officer's exercise of judgment and are contrary to long-established procedures.

(4) Shifting the Burden of Proof as to Cost Reasonableness to the Contractor. The FY 1986 Authorization Act overturns a legal precedent that costs incurred by a contractor are presumed to be reasonable. The long-standing "prudent businessman" test was upheld in court in the Bruce Construction case. In reversing this case, Con-

gress has deprived the courts and administrative boards of an accepted test for reasonableness.

We appreciate the opportunity to provide these additional comments. Please let me know if you need any further information.

Very truly yours,

KARL G. HARR, Jr.

REGULATORY PROCESS

Senator DIXON. Gentlemen, you each devote a large proportion of your statement to concerns about the manner in which the Department of Defense has implemented the 1984 defense procurement legislation.

To what extent have the difficulties that you describe resulted from lact of clarity in the original legislation is such areas as definitions, scope of coverage, et cetera?

Mr. HARR. The Defense Procurement Reform Act of 1984 was premised, in large part, on perceived problems in acquiring spare parts. While the bill was well intended, we do not believe the relatively few "horror stories" reported in connection with spares warranted statutory change of this scope. It ignored on-going efforts in the Department of Defense, beginning in 1983, to improve pricing, competition, use of economic order quantities, etc., in acquiring spare parts. It also ignored the recommendations made by the Office of Federal Procurement Policy in its report to the Congress in June 1984, following a Congressionally directed comprehensive review of DOD's spare parts procurement process, as well as the report and recommendations of the DOD Inspector General.

The problem is further compounded by the fact that the legislation covers all systems and not just spare parts. One area in particular where the bill is not clear is in the mater of an arbitrary time limit on a contractor's rights in data. Both the Air Force and the Navy had used clauses, prior to the enactment of this statute, which required a contractor to give up all rights in data after a specified period—in some cases five years and in others seven years. The DOD Study, "Rights in Data" completed in June 1984, concluded that: (1) arbitrary time limtis were not the answer to the data problem, and (2) only a very small percentage of the problem in getting more competition for replenishment parts was attributable to lack of rights in data. Nevertheless, the legislation stated that the Secretary of Defense could develop regulations and standards to guide contracting activities in attemtping, as a negotiation objective, to set a time limit on a contractor's rights in data. The sutatute states that this negotiation objective shall not exceed 7 years. This is being interpreted in many buying activities as an endorsement of the arbitrary time limits that DOD was using in the past. Another problem with this statute is that Congress directed the Secretary of Defense to implement the statute in the FAR system, i.e., in the DOD Supplement and not in the FAR itself. This adds to the proliferation of regulations. We are faced now with two sets of stand alone regulations on the subject of data rights, one for the civil agencies and one for the Department of Defense. There seems to be no reason why these regulations could not be substantially the same. The problem could have been avoided if Congress had directed a single implementation in the FAR.

Senator DIXON. What specific actions do you recommend that we take to introduce additional clarity into the legislation enacted over the past 2 years?

Mr. HARR. Congress could help a great deal to avoid proliferation of regulations, ambiguities in the regulations and conflicts in the regulations by requiring a single uniform implementation—in the FAR. Deviations or variations from that implementation would then be permitted only for demonstrated unique needs of a particular agency. The Defense Procurement Act requires the Secretary of Defense to publish proposed regulations in the Federal Register and to allow 30 days for public comment. However, this is a minimal period and generally occurs too late in the regulation cycle. There should be a requirement in the statute for early consultation with industry before policies are established and regulations written. Such policies and regulations are too important to be developed without the benefit of some input from those who will be most affected. It is obviously impossible for procurement personnel in the Federal Government to fully understand industry practices or the impact of new policies and regulations on these practices. Hence, it is important for regulation writers to consult with industry before promulgating rules and regulations. This kind of cooperation and consultation is not likely to occur without strong endorsement from Congress.

Senator DIXON. One strong general feeling that I get from all the witnesses is that there is not adequate and timely dialogue between the Department of Defense and the defense industry in the implementation process.

What steps can be taken to involve the industry and other affected parties at the front end of the rule-making process without adversely affecting the need for timely implementation of legislation.

Mr. **Harr**. The mention of need for timely implementation of legislation raises the question of "why the rush?" Obviously, legislation should be implemented within a reasonable time, but mandated deadlines for implementation must take into consideration the need to solicit industry and public views, hold open hearings, consider technical industry comments and, in some cases, allow time to test a policy, regulation or procedure before putting it into effect. Many of the deadlines for implementation contained in the Defense Procurement Reform Act were far too short to accomplish any, let along all, of the foregoing in a meaningful manner.

QUALITY ISSUES

Senator **Dixon**. Every one of you have underscored the need to emphasize quality in selecting sources for defense products. There seems to be a general perception that competition is now being based predominantly on price considerations to the detriment of quality.

What specific actions should we consider to more properly balance concerns for cost and quality in defense acquisition?

Mr. **Harr**. Emphasis on quality should not be used as an excuse to avoid competitive procurement; however, there has long been a failure by many in the Congress to recognize that there is effective competition already in negotiated procurement. Competition does not mean just formal advertising or sealed bid procurements. One problem arises from the requirement in the Competition in Contracting Act for "full and open" competition in all cases. This can, and does, stretch out and complicate the process and leads to awards to marginal firms. One solution would be to give the contracting officer more flexibility to select qualified firms with whom to carry on negotiations, particularly where quality or performance characteristics are especially critical.

Senator **Dixon**. How should we define quality criteria so that the wisdom of making a contract award on the basis of quality rather than price is readily apparent?

Mr. **Harr**. Quality criteria should be considered in connection with life cycle costs and also in connection with criticality of usage. If equipment is to be operated in an environment where replacement parts are readily available and can be quickly installed, or continuous operation of the equipment is not critical, it may not be a serious matter if parts have to be replaced at frequent intervals or if there are frequent disruptions of service. However, with such items as sophisticated electronics equipment used in critical defense hardware, quality is paramount if equipment is to perform its intended mission. In such cases, factors such as mean time between failure, zero defects, mean time to repair, etc., should be weighted appropriately in source selection.

WARRANTIES

Senator **Dixon**. On the specific issue of warranties, concerns have been expressed that warranties are being required without regard to technical risk or cost. During our October 17 hearing with Dr. Wade, we raised the issue of cost/benefit analysis and the use of the statutory waiver authority.

How do you view the fact that only minimal use is being made of the authority to waive warranty requirements on defense contracts?

Has it been the experience of your member companies that the Services are conducting thorough cost/benefit analyses in weighing their decision of whether to require a warranty for a given product?

One of the concerns I have heard expressed is that each of the Services are "going their own way" on warranty policy.

In your view, what are some of the inconsistencies in the manner in which the Services have implemented the warranty legislation?

Mr. **Harr**. The following comments respond to all three of the questions on warranties. Our experience with the new warranty requirements is limited. In general, implementation of the warranty provisions in the buying activities appears to be progressing satisfactorily, considering the legislation effective date, the lack of implementation guidance to the agencies, and the necessary learning curve problems associated with any new contractual requirement. As I noted in my statement, the fact that only one waiver has been requested, to our knowledge, suggests the likelihood that the government is demanding warranties on all programs, even where they may not be cost effective. It may be that the time needed to obtain Congressional waiver would cause unacceptable delay in the procurement cycle where urgent program decisions are mandatory. In the long run, only time and experience by both parties will determine the appropriateness and effectiveness of warranties.

AUTHORITY AND ACCOUNTABILITY IN THE ACQUISITION WORK FORCE

Senator **Dixon**. Mr. Harr, you make the point at the end of your statement that one test for legislative proposal should be how well they clarify the "proper roles and functions of the various parties in the procurement process."

Would you apply this general principle to the recently passed legislation and give us an industry perspective on how well the specific legislative provisions meet this test?

Mr. **Harr**. We assume that by "recently passed legislation" you include the procurement reform provisions in the fiscal year 1986 DOD Authorization Act. These go even further than the 1984 legislation in failing to recognize the proper roles and functions of various parties in the procurement process. Whether intentional or not, one result of most of this legislation is to aggrandize the role of the auditor and, at the same time, diminish the authority and responsibility of the contracting officer. In many cases, the contracting officer becomes a rubber stamp for auditors' determinations. In a broader sense, the legislation inhibits the flexibility of the Executive Branch in determining how best to provide for defense needs. For example, it requires full and open competition in all cases and does not provide for the concept of effective competition among qualified sources. Finally, and more importantly from our standpoint, the legislation micromanages the acquisition process. It erodes, if not destroys, the concept of reasonableness in pricing and dictates to industry, in minute detail, elements of costs that may or may not be allowed. Another area that I would like to mention here is the matter of work measurement which is covered in the fiscal year 1986 Authorization Act. The controversy that has surrounded this particular provision points up the fact that it is a very complex subject and one which cannot be handled through the simplistic solution dictated by the Authorization Act. There is need for Congressional hearings and for much more depth of understanding on this subject before legislation is enacted.

Questions Submitted by Senator John Glenn

Senator **Glenn**. During the past 2 weeks we have heard several witnesses from DOD, including Dr. Wade, testify that there have been serious problems implementing the 1984 legislation and that Congress should resist further procurement reform legislation until they have had time to fully access the impact of the 1984 legislation.

Now, I see several of you from industry are recommending the same thing.

Since this course of action is not realistic, and given the scope of the proposed 1985 procurement reform legislation, can you give us your views on what impact the passage of all or most of the 1985 legislation will have on the efficiency of the DOD acquisition system?

Mr. **Harr**. If, by 1985 legislation, you mean the procurement reforms attached to the fiscal year 1986 DOD Authorization Act, these will add further to reporting requirements, audit requirements, and the atmosphere of regulatory and procedural gridlock.

Senator **Glenn**. I was very interested in your statement, Mr. Harr, that:

Congress is taking away the best means of ensuring that the nation gets the latest technologies and the most for every dollar spent on defense. In fact, it is taking away one of the principal assets it is paying for—the managerial capability of its suppliers.

Would you elaborate on this statement, please.

Mr. **Harr**. The Department of Defense does business with almost all of the major firms in the United States. The managerial capability of these firms is attested to by their success in building and operating multi-billion dollar companies. However, their management decisions are now being second-guessed as never before—their talents in effect wasted by DOD's over-emphasis on audits, inspections and other reviews. The concept or reasonableness with respect to cost—what a prudent businessman would do—is virtually meaningless under present statutes. As Senator Goldwater noted earlier, only a handful of the people who are passing laws have had that industry experience essential to well-considered legislative action on these matters.

Senator GLENN. Dr. Wade testified that quality was on the top of his agenda for the future. He stated that in DOD acquisition, competition is too frequently based on price and an "award to the low bidder" mentality is too expensive.

Dr. Wade indicated that DOD plans to move away from defining equipment requirements in minimally acceptable terms to a system whereby the best quality equipment at an acceptable price is their recognized objective.

My observations have been that there has been too much emphasis on cost at the expense of quality. I would appreciate your comments on cost versus quality as related to current procurement regulations.

Mr. HARR. Although this has been discussed earlier, I would add that the Uniform Procurement System proposal presented to the Congress by the Administration in 1982 included the concept of effective competition. In the course of the legislative cycle this was changed to "full and open" competition, which invites marginal or unqualified offerors and makes it much more difficult for the contracting officer to exercise judgment in weighing quality versus cost. It would be desirable to establish pre-qualified lists of offerors wherever quality is a critical factor. This can be done while still retaining effective competition.

Senator GLENN. We have heard testimony that dual sourcing is an excellent technique for reducing program risk and production costs in selected situations, but it is not the panacea that current legislative proposals would lead one to believe.

I also read recently where the Navy has issued an order directing that all new weapons programs will have two sources.

I would appreciate your comments on the value of dual sourcing, both the leader-leader approach and the leader-follower approach.

Mr. HARR. Dual Sourcing is fine if you are assured of sufficient production quantities throughout the life of a program to warrant duplicate start up costs. It is also useful for purposes of establishing a mobilization base even in instances where it may not be the most economical method of conducting a procurement. However, where start up costs are very high and production quantities are insufficient or uncertain, it may be counterproductive or impracticable to establish two sources just to have downstream competition.

Senator GLENN. There has been concern expressed that procurement reforms have curbed the flexibility and authority of program managers. It has been suggested that several pilot programs be identified where most regulations could be waived and managers given a free hand.

The goal would be to see what managers could do if instructed to "use good management and common sense."

Do you believe this would be a worthwhile project?

Mr. HARR. It may be going too far to tell a manager simply to "use good judgment and common sense" and not give any further regulatory guidance or instructions. However, we have certainly gone too far in the other direction. Any approach that will give contracting officers and program managers, as well as industry managers, appropriate room to exercise managerial flexibility and judgment so that they may be held accountable for the results they achieve, is worth pursuing.

QUESTIONS SUBMITTED TO MR. VICO HENRIQUES, PRESIDENT, COMPUTER AND BUSINESS EQUIPMENT MANUFACTURERS ASSOCIATION

JANUARY 10, 1986.

Hon. DAN QUAYLE,
Chairman, Subcommittee on Defense Acquisition Policy, Committee on Armed Services, U.S. Senate, Washington, DC.

DEAR MR. CHAIRMAN: At the conclusion of my testimony before your Subcommittee on November 7, 1985 you asked CBEMA to send you a legislative "wish list" of needed remedies to recent procurement legislation.

Attached you will find our input on this vitally important subject. CBEMA, and I am sure others, view the work of your Subcommittee as critical to the improvement of the defense acquisition process.

At that time, we requested and received an extension for our responses to the questions submitted for the record. Our answers to those questions are enclosed.

CBEMA has for convenience numbered each of the questions in sequence, one (1) through eighteen (18). Further, we have followed the subject matter breakdown as presented in questions submitted to us as follows:

General—Question 1.
Regulatory Process—Questions 2, 3, 4, and 5.
Quality Issues—Questions 6 and 7.

Warranties—Questions 8, 9, and 10.
Data Rights—Question 11.
Commercial Pricing—Question 12.
Authority and Accountability in the Acquisition Workforce—Questions 13, 14, 15, 16, 17, and 18.

As you will see when reviewing our submission, certain of the questions clearly deal with areas that we consider CBEMA well qualified to answer in detail. Others will be responded to briefly or not at all, depending on the nature of the question.

Where appropriate we will make specific recommendations for legislative actions we feel are necessary to improve the acquisition process.

Very truly yours,

VICO E. HENRIQUES, *President.*

DEFENSE PROCUREMENT REFORM ACT OF 1984 (P.L. 98-525)

A. 10 U.S.C. 2323—Commercial pricing for supplies

1. Problem.—Application of the provision beyond spare and replenishment parts.

Background.—Congressional hearings and the House and Senate legislation that passed and went to conference concerned "replenishment and spare parts." For some unexplained reason, the conference version (which became enacted into law) substituted "supplies" or "items of supply." The conference report, despite this change, referred to replenishment and spare parts as the subject matter—consistent with the earlier committee hearings and the House and Senate action.

Solution.—By legislative enactment, modify section 2323 so as to make it clear that its thrust and application is only to "replenishment and spare parts," which should be precisely defined.

2. Problem.—The present wording (e.g., "offered for sale to the public," "lowest price at which such items are sold by the contractor to the public," and "lowest commercial price") encompasses marketing classifications other than end-users, the customer category which the government occupies.

Background.—There are items (supplies) which are sold by the manufacturer in a functional marketing setting in addition to end-user customers. Sales to dealers, distributors and original equipment manufacturers (OEMs) are customer classes where the purchaser is (i) buying for resale and (ii) adds further manufacturing, service or marketing (e.g., warehousing, sales, etc.) value before resale to the ultimate end-user.

Solution.—The section should be modified so that the certification requirements of subsections (a) and (b) encompass only end-user commercial sales for purposes of comparison, justification and certification. In the same contect, subsection (c) should be clarified; the following rewritten subsection (c) is offered:

(c) The phrases "to the public" and "lowest commercial price," as used in subsections (a) and (b), only encompass sales to end-user customers but exclude sales to the Government, as well as sales to affiliates, subsidiaries or divisions of the offeror. Moreover, subsections (a) and (b) do not apply to a contract if the contracting officer determines that use of the price otherwise required by subsection (a) for such contract is not appropriate because of (1) national security considerations; or (2) differences in quantities, quality, delivery, or other terms and conditions of the prospective contract from the offeror's commercial end-user contract terms.

3. Problem.—As written, section 2323 does not include a de minimis concept; a "floor" on the need for certifying. Consequently, a sale of $5 carries the same administrative burden as a $5,000 spare parts order.

Background.—Unlike the usual certification requirements established by Congress (e.g., Truth in Negotiation Act with its $100,000 threshold requirement), section 2323 does not recite a dollar amount which, if exceeded, requires execution of the certificate.

Solution.—Modify section 2323 to make it only mandatory on spare or replenishment part contracts that exceed $1,000 in total award amount.

B. Section 1245 of P.L. 98-525—Regulations for allocating overhead to parts to which the prime contractor has added little value

Problem.—As broadly drafted, section 1245 unnecessarily and adversely impacts commercial product suppliers (manufacturers and regular dealers) who were not the cause of the problem that prompted the legislative enactment.

Background.—A review of the legislative history (e.g., Conference Report 98-1080) clearly indicates that Congress was concerned about the purchase of parts and common items outside the normal commercial distribution channels, coupled with the addition of overhead charges all out of proportion to the intrinsic work of the services rendered, as reflected by the overhead "adder." The $7 hammer that carried an ultimate sale price to the Government of $435 was the classic example. Section 1245 requires the prospective contractor to (i) indicate his overhead allocation method and (ii) identify supplies to which the contractor did not contribute significant value. Again, these two questions are appropriate to the weapon system contractor who is reselling the aforementioned hammer. We submit section 1245 is inappropriate and should not apply to contractors who are manufacturers and/or regular dealers of commercial items.

Solution.—Amend section 1245 to specifically exempt, as offerors and prime contractors, manufacturers and regular dealers of commercial items.

C. 10 U.S.C. 2384—Supplies: Identification of supplier and sources

Problem.—As drafted, subsections (b) and (c) grant the Secretary of Defense a measure of discretion in implementing the language of these two subsections. However, the proposed implementation from the DAR Council (case number 85-66) failed to exercise the obvious judgment of excluding commercial products from its application.

Background.—The new section 2384 was prompted by a desire to obtain from the weapon system manufacturer (prime contractor) his sources of supply for components and parts so the Government could "purchase the item directly from the manufacturer or producer and avoid the middleman" (quoting from p. 322 of Conference Report 98-1080). While the information sought in subsection (b) is appropriate when the hardware is specially designed and manufactured for the DOD, it is clearly wrong to apply subsection (b) to supplies designed, manufactured and offered for sale to the commercial marketplace. For example, there is no valid reason to impose on a commercial electric typewriter manufacturer questions indicating whether certain spare parts are "made," "bought," or both. Unfortunately, in its proposed implementation of subsection (b), the DAR Council failed to exercise the available discretion so as to remove this burden from commercial product manufacturers.

Solution.—Amend 10 U.S.C. 2384, subsection (b) so as to make it clear that its provisions shall not apply to "supplies that are designed, manufactured and offered for sale to the commercial marketplace."

D. 10 U.S.C. 2320—Rights in technical data

Problem.—Unlike its civilian agency counterpart (see section 301 of P.L. 98-577), section 2320 does not contain within its text certain policy statements that are vitally important to commercial product manufacturers. We refer to section 1202, subsection (6) of P.L. 98-525.

Background.—Our industry was concerned that technical data relating to products and processes sold to the general public (i.e., commercially oriented items) would be demanded and furnished to the DOD as a condition of contract award. In the hurried, final days of "mark-up" and passage, rather than amending the soon-to-be adopted section 2320, "comfort language" was included as subsection (6) to section 1202, "Congressional Findings and Policy." In drafting the regulation to implement section 2320 (which was subsequently withdrawn for further study), the DAR Council gave no recognition whatsoever to the aforementioned subsection (6) policy language. Informal discussions with DOD representatives indicated that, as far as they were concerned, subsection (6) had no force and effect. This attitude, coupled with the section 2320, subsection (c) provision—which permits DOD to place a "cap" on its protection of a contractor's technical data rights—convinces us that DOD intends to treat everyone as if they were all weapon systems designers and hardware suppliers. In essence, the commercial product technical data receives no separate consideration.

Solution.—(1) Section 2320 should be amended to include within its subsection (a) the aforementioned policy language. See in this regard section 301 of P.L. 98-577.

(2) We also recommend the repeal of section 2320, subsection (c), the authorizing "cap" provision on protection of contractor and subcontractor privately developed technical and proprietary data. This provision is a "blank check" permitting overzealous implementation by the DOD services (e.g. Air Force and Navy) without proper analysis and regard for the negative impact it will have on commercially oriented suppliers' continued support of defense programs. The adverse "price" to such suppliers is loss of their technical data rights. We must emphasize that the prime contractor (weapon system integrator) will find lower-tier vendors and suppliers refusing to take the "pass-on" of such onerous provisions. In the final analysis, the best, brightest and most innovative suppliers will be "driven away" from applying their commercially-derived talents to DOD programs.

SMALL BUSINESS AND FEDERAL PROCUREMENT COMPETITION ENHANCEMENT ACT OF 1984 (P.L. 98-577)

A. Section 204—Commercial pricing for supplies

Problem.—The same lack of clarity and proper application present in Section 2323 of P.L. 98-525 exists in this Section 204.

Background.—P.L. 98-577 was enacted eleven days after P.L. 98-525. The Defense bill took the lead in fashioning the language; consequently, the "flaws" enacted in Section 2323 were adopted *in toto* within Section 204.

Solution.—Adopt the same three recommended amendments to 10 U.S.C. 2323, so that Section 204 is similarly corrected.

B. Section 501—Regulations on overhead

Problem.—The same misapplication to offerors who are commercial product manufacturers and dealers, as was enacted in the Defense bill's identical counterpart—Section 1245 of P.L. 98-525.

Solution.—Enact the same recommended change to Section 501 as is proposed for Section 1245.

C. Section 302—Publication of proposed regulations

Problem.—This section, which is intended to provide industry adequate notice and opportunity to comment on new procurement policies and regulations, is not being implemented in the manner we believe Congress envisioned. The exception (urgent and compelling circumstances) has been abuysed and misapplied so as to effect rules upon industry without being accorded the customery notice and 30-day minimum comment period.

Background.—Recent actions by the DOD indicate an inability, or unwillingness, to meet wither the spirit or letter of Section 302. A most notable example was Secretary Weinberger's mandated overhead cost certification policy, it was effective upon issuance with no prior notice and comment from industry. In the same vein, the Federal Acquisition Regulation Council issued Circular FAC 84-10 under the "urgent and compelling circumstances" exception. It should be noted that the statutory provisions implemented by FAC 84-10 took effect 6 months after enactment—about April 19, 1984; yet the implementing regulations (Item II and III of Fact 84-10) were not issued until July 3, 1985. Consequently, the FAR Council consumed nine months time, was delinquent, and used the exception to immediately implement its work product. Items II and III of FAC 84-10, as issued, have presented major implementing problems, no doubt caused in part by lack of dialogue and discourse through normal rulemaking. This experience fosters our belief that FAC 84-10, Items II and III must be effectively remedied through clarifying legislation, which was detailed earlier.

Solution.—Through oversight hearings, Congress should examine the use of the "urgent and compelling circumstances" exception of Section 302. Where there is a combination of (i) a stringent effective date for a legislative enactment, and (ii) lack of agency time and/or resources to issue implementing regulations with proper regard for the rulemaking process, then it seems appropriate to consider an extension to the law's effectivity date.

DEFENSE PROCUREMENT IMPROVEMENT ACT OF 1985 (P.L. 99-145)

Background.—Section 911 created a new Section 2324 to Title 10 of the U.S. Code. Subsection (e) listed 10 specific cost elements as unallowable; subsection (f) directed the DOD Secretary to define and clarify 16 other cost elements. At the present time, the FAR Council is undertaking these revisions; it should be noted that Section 911 applies only to DOD, yet the FAR Council intends to make the new regulations government-wide (i.e., civilian agencies) for the sake of uniformity.

Recommendation.—Through Subcommittee oversight action, the wisdom of these actions should be reviewed. A particular focus should be this question: by disallowing cost elements that are allowable in the commercial world and recognized as valid business expenses, is the Government discouraging commercially-oriented business from participating in this environment with its "dual accounting" concepts? As a further extension of this forced dualism, consider the recently adopted "Federal Civilian Employee and Contractor Travel Expenses Act of 1985." A commercial company can have reasonable and prudent policies and procedures for reimbursing its employees for travel on company business. However, if this same company takes a government contract which requires travel in its performance, reimbursement will be limited to the special rules mandated by this Act. Again, a dual accounting and reimbursement concept is forced upon the commercially-oriented vendor.

QUESTIONS SUBMITTED BY SENATOR ALAN DIXON

1. General

Senator **DIXON**. On October 29, the Joint Logistics Commanders testified before our Subcommittee. I would like to put one of the same questions to you that we asked of them. Which acquisition legislation currently in effect would you like to see modified or repealed?

Mr. **HENRIQUES**. In our testimony we expressed serious concern with regard to the "Certification of Commercial Prices" of Federal Acquisition Circular 84-10 (FAC 84-10), which implements PL 98-525 and PL 98-577. We believe the following legislative remedies are necessary in order to finally resolve the problems:

—Clarify that the Certificate for Commercial Pricing applies only to spare and replacement parts.

—Clearly limit the use of the certificate to procurements where full and open competition is not used as the acquisition procedure.

—Clearly limit the price comparison in the Certificate to "the lowest price charged any domestic commercial end-user customer." This would define the class of customer which is appropriate for price comparison/certification purposes and would remove from the comparison inappropriate classes of customers such as dealers, distributors and original equipment manufacturers (OEMs).

—Delete any requirement for proprietary cost or pricing data submissions not otherwise required by law.

In the matter of the "Integrity of Unit Prices" section of FAC 84-10, we recommend that commercial product manufacturers and regular dealers be exempt from these rules, based upon the fundamental differences between the government-designed product and commercial product marketplaces.

We have noted our serious concern with the encroachment on the legitimate rights of private industry, especially the commercial product side of private industry, in the area of technical data rights. We propose the following legislative remedies:

Clearly emphasize the distinction between cost-type and commercial products and the protections which are therefore afforded technical data associated with products "developed at private expense."

Provide alternatives to the "time limit for expiration of limited rights."

Recognize and provide for a proper balance between the government's needs and industry's just rights.

Provide protection for the legitimate intellectual property rights of commercial product manufacturers.

2. Regulatory process

Senator **DIXON**. Gentlemen, you each devote a large proportion of your statement to concerns about the manner in which the Department of Defense has implemented the 1984 defense procurement legislation. To what extent have the difficulties that you describe resulted from lack of clarity in the original legislation in such areas as definitions, scope of coverage, et cetera?

Mr. **HENRIQUES**. To a fair degree at least the genesis of the problems that the high tech commercial product industry has had with DOD's implementations of the 1984 legislation ties back to lack of clarity in the original legislation. For example, in the case of the Certification of Commercial Pricing requirements of FAC 84-10 a base question is the proper scope of coverage. Congressional hearings and the House and Senate legislation that passed and went to conference concerned "replenishment and spare parts." For some unexplained reason, the conference version (which became enacted into law) substituted "supplies" or "items of supply." The conference report, despite this change, referred to replenishment and spare parts as the scope of coverage--consistent with the earlier committee and House and Senate action. The change to "supplies" and "items of supply" causes a dramatic increase in the information and paperwork burden placed upon the high tech commercial product industry. Furthermore, it shifts the main thrust of the regulatory implementation away from the prime problem that the Congress set out to fix, that is, the alleged horror stories in DOD's procurement of replenishment and spare parts.

A similar problem exists in Section 1245 of P.L. 98-525: Regulations for Allocating Overhead to Parts to Which the Prime Contractor Has Added Little Value. As broadly drafted, Section 1245 unnecessarily and adversely impacts commercial product suppliers (manufacturers and regular dealers) who were not the cause of the problem that prompted the legislative enactment. A review of the legislative history (e.g. Conference Report 98-1080) clearly indicates that Congress was concerned about the purchase of parts and common items outside the normal distribution channels, coupled with the addition of overhead charges completely out of proportion to the intrinsic value of the services rendered by the party providing the part or common item to the DOD. The $7 hammer that carried the ultimate sale price to the government of $435 was the classic example. This problem is solved by having regulatory control of the weapon system contractor who is reselling the $7 hammer, but not by subjecting the manufacturer of the $7 hammer to unwarranted regulatory intrusion as is the case in the current regulatory implementation. Section 1245 should have averted this problem by clearly stating that it did not apply to contractors who are manufacturers and/or regular dealers of commercial items.

I will not go into other areas of this clarification problem at this point, but we have addressed them in the legislative "wish list" which we are submitting at Senator Quayle's request.

3. Senator DIXON. What specific actions do you recommend that we take to introduce additional clarity into the legislation enacted over the past two years?

Mr. HENRIQUES. In future procurement legislation, it is essential that clear distinctions be made between rules for the acquisition of special-design products and those for the acquisition of commercial, off-the-shelf products.

The rules for commercial product procurement must by definition be significantly different from those for government-design produts. In the commercial product business, the research, development, manufacture, etc. are at private expense and risk. The products are developed by the companies for a very broad market in which the Government is only one of the buyers—perhaps a significant buyer, but certainly not the dominant buyer. In the special-design product business, the Government funds the development, design, and manufacture of the product for its specific needs—because it is the ONLY buyer of that specific product.

The commercial system works to produce highly competitive products at low prices. The Government has long recognized that it can save taxpayer money by buying commercial products whenever possible, rather than specially-designed products.

The focus of Congress in its procurement reform legislation has not been on the commercial product side of the equation, but on the cost-type products, especially spare and replacement parts. However, the commercial product industry is being seriously affected by the new laws because the Defense Department, in its implementation of those reforms, is requiring access to commercial product producers' cost information. This is an entirely improper government intrusion into free enterprise business. The philosophy seems to be that a company should surrender its basic proprietary business data simply because it sells its commercial products to the Government. This could be viewed as an attempt to nationalize private sector commercial product business.

4. Senator DIXON. Mr. Rittenhouse, in your testimony you state: "We believe that it is incumbent on Congress to ensure uniform, concise and timely dissemination and implementation of legislative reforms." This sentiment has been echoed by all the witnesses here today. What specific actions should the Subcommittee be considering to achieve this goal?

Mr. HENRIQUES. Senator Dixon, I'd like to make a comment relative to your question to Mr. Rittenhouse on specific actions the Subcommittee should be considering to achieve the goal of uniform, concise, and timely dissemination and implementation of legislative reforms. First of all, I believe the Subcommittee must maintain a continuous cognizance of the procurement reform activities of the other relevant committees of the Congress to ensure that whenever possible differing and/or conflicting statutory provisions are not enacted. For example, we believe that some of the current confusion in the technical data rights area comes from differing provisions in P.L. 98-525 and P.L. 98-577.

Second, I think the Subcommittee must be vigilant to ensure that statutory language is explicit and clear enough to preclude varying interpretations by differing implementing organizations.

Finally, I think the Subcommittee should consider legislating provisions which would require the regulators to review their implementation concepts with the Congress early in the process and to provide proposed regulations to the Congress for review prior to issuing any interim rules or final regulations. These provisions should also provide for discussions between the regulators and industry early in the implementation process.

5. Senator DIXON. One strong general feeling that I get from all the witnesses is that there is not adequate and timely dialogue between the Department of Defense

and the defense industry in the implementation process. What steps can be taken to involve the industry and other affected parties at the front end of the rule-making process without adversely affecting the need for timely implementation of legislation?

Mr. **Henriques**. I believe it should be possible for the FAR Councils to have discussions with industry early in the rule-making process as to the concept of implementation, before any detailed regulatory writing begins. For example, in FAC 84-10, there was no industry/government dialogue prior to implemenation of the regulation. Therefore, we were unable to warn them in advance that what they proposed was simply unworkable in the commercial product arena. Open and cooperative discussions at an early point could go far in defining what might be feasible, practicable, and equitable in implementation. Ironing out such questions early in the process could avoid major pitfalls and delays later on. I think this clearly could have been the case in FAC 84-10.

6. Quality issues

Senator **Dixon**. Every one of you have underscored the need to emphasize quality in selecting sources for defense products. There seems to be a general perception that competition is now being based predominantly on price considerations to the detriment of quality.

What specific actions should we consider to more properly balance concerns for cost and quality in defense acquisition?

7. Senator **Dixon**. How should we define quality criteria so that the wisdom of making a contract award on the basis of quality rather than price is readily apparent?

Mr. **Henriques**. Senator Dixon, let me comment on the two questions on the quality issue. Our industry produces commercial products that must pass the test of satisfactory performance in a market-oriented economy. It is incumbent on our industry to produce quality products that we can warrant and maintain under a fixed price contract. Reliable products sell in the future. If the products of our industry do meet this criteria they are successful; if not, they aren't.

As we do not produce defense products that are designed to government specification we are not qualified to comment on quality practices of the DOD. Our experience in the utilization of commercial products by the Government as a whole, including DOD, is that the market test described above prevails.

8. Warranties

Senator **Dixon**. On the specific issue of warranties, concerns have been expressed that warranties are being required without regard to technical risk or cost. During our October 17 hearing with Dr. Wade, we raised the issue of cost/benefit analysis and the use of the statutory waiver authority. How do you view the fact that only minimal use is being made of the authority to waive warranty requirements on defense contracts?

9. Senator **Dixon**. Has it been the experience of your member companies that the Services are conducting thorough cost/benefit analyses in weighing their decision of whether to require a warranty for a given product?

10. Senator **Dixon**. One of the concerns I have heard expressed is that each of the Services are "going their own way" on warranty policy. In your view, what are some of the inconsistencies in the manner in which the Services have implemented the warranty legislation?

Mr. **Henriques**. Senator Dixon, again let me comment on your three questions on warranties. Our members produce and market commercial products; thus we are not qualified to comment on weapon system warranty issues in any detail, since commercial products are exempt from legislation that requires warranties for defense products.

We would like to commend the Congress for the exemption referred to above. The 1984 legislation required commercial products to warrant to government design. No company could in good conscience make such a warranty since commercial products are not designed for government requirements. Furthermore, the development and detailed design are based upon the requirements of a broad commercial marketplace and are finalized long before the government solicits for its needs.

11. Data rights

Senator **Dixon**. Mr. Stewart, you make the statement in your testimony that the new statutory provisions governing rights in technical matters "may be defective in certain respects" and you encourage our Subcommittee to reexamine it. You give one specific example in your statement, that of the "cap" on the length of time that data restrictions would apply.

What are other areas we should be monitoring? Do any of the other witnesses have any suggestions?

Mr. HENRIQUES. As we stated in response to your first question, we have noted our serious concern with the encroachment on the legitimate rights of private industry, especially the commercial product side of private industry, in the area of technical data rights. We propose the following legislative remedies:

Clearly emphasize the distinction between cost-type and commercial products and the protections which are therefore afforded technical data associated with products "developed at private expenses."

Recognize and provide for a proper balance between the government's needs and industry's just rights.

Provide protection for the legitimate intellectual property rights of commercial product manufacturers.

12. Commercial pricing

Senator DIXON. Mr. Henriques, you devote the majority of your written testimony to the issue of commercial pricing addressed in Federal Acquisition Circular 84-10. You mention several concerns, such as fundamental differences between cost-based, unique defense products and commercial products, lack of industry-DOD dialogue, and additional costs for the collection of data.

Could you provide our Subcommittee with some specific courses of action that we might take to help sort out these issues?

Mr. HENRIQUES. In response, let me refer you to my answer to your third question. I would like also to submit at this point CBEMA's detailed response to Senator Quayle's request for a legislative "wish list."

13. Authority and accountability in the acquisition work force

Senator DIXON. Mr. Harr, you make the point at the end of your statement that one test for legislative proposals should be how well they clarify the "proper roles and functions of the various parties in the procurement process."

Would you apply this general principle to the recently passed legislation and give us an industry perspective on how well the specific legislative provisions meet this test?

(No CBEMA response.)

QUESTIONS SUBMITTED BY SENATOR JOHN GLENN

(The questions attributed to Senator Glenn to be answered for the record are as follows:)

Senator GLENN. During the past two weeks we have heard several witnesses from DOD, including Dr. Wade, testify that there have been serious problems implementing the 1984 legislation and that Congress should resist further procurement reform legislation until they have had time to fully assess the impact of the 1984 legislation.

Now, I see several of you from industry are recommending the same thing. Since this course of action is not realistic and given the scope of the proposed 1985 procurement reform legislation, can you give us your views on what impact the passage of all or most of the 1985 legislation will have on the efficiency of the DOD acquisition system?

Mr. HENRIQUES. The 1985 procurement legislation mandated a variety of changes, additions, etc. to the current acquisition system. These changes essentially deal with the cost-based weapons system, an area where we are not expert.

Our experience relating to 1984 procurement reform leads us to the conclusion that 1985 procurement reform legislation will not substantially increase the efficiency of the DOD acquisition system. In fact the reverse is likely. The DOD when developing regulations almost always exceeds what the Congress has legislated. This is especially true when it comes to acquisition of commercial products. The DOD insists on meshing commercial product acquisition with cost-based defense products which serves neither the best interests of industry, government, nor the taxpayer.

Specifically our views on what might be done to improve the 1985 package are best illustrated by analysing Section 911 of P.L. 99-145, as follows:

DEFENSE PROCUREMENT IMPROVEMENT ACT OF 1985 (P.L. 99-145)

Background.—Section 911 created a new Section 2324 to Title 10 of the U.S. Code. Subsection (e) listed 10 specific cost elements as unallowable; subsection (f) directed the DOD Secretary to define and clarify 16 other cost elements. At the present time, the FAR Council is undertaking these revisions; it should be noted that Section 911 applies only to DOD, yet the FAR Council intends to make the new regulations government-wide (i.e., civilian agencies) for the sake of uniformity.

Recommendation: Through Subcommittee oversight action, the wisdom of these actions should be reviewed. A particular focus should be this question: By disallowing cost elements that are allowable in the commercial world and recognized as valid business expenses, is the government discouraging commercially-oriented business from participating in this environment with its "dual accounting" concepts? As a further extension of this force dualism, consider the recently adopted "Federal Civilian Employee and Contractor Travel Expenses Act of 1985." A commercial company can have reasonable and prudent policies and procedures for reimbursing its employees for travel on company business. However, if this same company takes a government contract, which requires travel in its performance, reimbursement will be limited to the special rules mandated by this Act. Again, a dual accounting and reimbursement concept is forced upon the commercially-oriented vendor.

15. Senator **Glenn**. I was very interested in your statement, Mr. Harr, that: "Congress is taking away the best means of ensuring that the nation gets the latest technologies and the most for every dollar spent on defense. In fact, it is taking away one of the principal assets it is paying for—the managerial capability of its suppliers."

Would you elaborate on this statement, please.

(No CBEMA response.)

16. Senator **Glenn**. Dr. Wade testified that quality was on the top of his agenda for the future. He stated that in DOD acquisition, competition is too frequently based on price and an "award to the low bidder" mentality is too expensive.

Dr. Wade indicated that DOD plans to move away from defining equipment requirements in minimally acceptable terms to a system whereby the best quality equipment at an acceptable price is their recognized objective.

Mr. observations have been that there has been too much emphasis on cost at the expense of quality. I would appreciate your comments on cost versus quality as related to current procurement regulations.

Mr. **Henriques**. Senator, I would suggest that the government should place increased emphasis on lowest-total-overall-cost procurements, moving the government away from its very costly reliance on evaluation practices which over-emphasize initial low-bid prices. Procurement evaluations which recognize true life-cycle costs as the more significant acquisition determinant inherently cause the government to procure quality products.

17. Senator **Glenn**. We have heard testimony that dual sourcing is an excellent technique for reducing program risk and production costs in selected situations, but it is not the panacea that current legislative proposals would lead one to believe.

I also read recently where the Navy has issued an order directing that all new weapons programs will have two sources.

I would appreciate your comments on the value of dual sourcing, both the leader-leader approach and the leader-follower approach.

(No CBEMA response.)

18. Senator **Glenn**. There has been concern expressed that procurement reforms have curbed the flexibility and authority of program managers. It has been suggested that several pilot programs be identified where most regulations could be waived and managers given a free hand.

The goal would be to see what managers can do if instructed to "use good management and common sense."

Do you believe this would be a worthwhile project?

(No CBEMA response.)

In addition to my answers to the questions submitted for the record, as indicated in my previous response on page 66 of the transcript, I would like to add the following comments:

Senator Levin, at the November 7, 1985 hearing, you queried Mr. Rittenhouse as to the detailed circumstances of an OMB disapproval mentioned in his statement. While there were some oral discussions by the various members of our panel at the time, I would like to provide the following expansion:

Under the provisions of the Paperwork Reduction Act of 1980 (44 U.S.C. Chapter 35), the Federal Acquisition Regulation (FAR) Secretariat on June 25, 1985 submitted to OMB a request to review and approve a new information collection. This request covered the collection of information to be used in the certification of commercial pricing as required by Sec. 204 of P.L. 98-577 "Small Business and Federal Procurement Competition Enhancement Act of 1984" and Sec. 1216 of P.L. 98-525 "Defense Procurement Reform Act of 1984." The regulatory implementation of these sections was published as an immediately effective interim rule in the Federal Register of July 3, 1985 as Item III—Certification of Commercial Pricing—of Federal Acquisition Circular 84-10 (FAC 84-10). A public notice of the FAR Secretariat's request to OMB appeared in the Federal Register of July 2, 1985, inviting the submission of public comments on that information collection requirement to OMB.

In response to the Federal Register notice of July 2, 1985, CBEMA obtained a copy of the Information Collection Request from the FAR Secretariat, and after analyzing it and FAC 84-10 began having dialogue with and making submissions to the Office of Information and Regulatory Affairs (OIRA) in OMB. Other associations and a number of companies initiated similar efforts. Included in CBEMA's dialogue with OIRA was a meeting with its Acting Administrator on September 17, 1985.

After consideration of the public comments and meeting with the FAR Councils, OMB disapproved the FAR Secretariat's Information Collection Request on September 25, 1985. Following is a quotation from the remarks section of that disapproval:

"Disapproved because the practical utility of the reporting and recordkeeping requirements has not been shown. No justification has been provided for requiring vendors to justify their lowest price charged to any customers when the statute calls for comparison to lowest commercial price. Furthermore, the practical utility of requiring data about how prices for commercial items are developed has not been shown."

In effect, OMB's disapproval was based upon the FAR Councils' unjustified regulatory expansions beyond the provisions of the laws. OMB and the FAR Councils are still in the process of trying to resolve these issues.

[Whereupon, at 11:55 a.m., the subcommittee adjourned, to reconvene on Wednesday, November 13, 1985.]

IMPLEMENTATION OF THE 1984 DEFENSE PROCUREMENT

WEDNESDAY, NOVEMBER 13, 1985

U.S. SENATE,
COMMITTEE ON ARMED SERVICES,
SUBCOMMITTEE ON DEFENSE ACQUISITION POLICY,
Washington, DC.

The subcommittee met in open session, pursuant to notice, at 10:27 a.m., in room SD-342, Dirksen Senate Office Building, Senator Dan Quayle (chairman) presiding.

Present: Senators Quayle, Warner, Levin, Bingaman, and Dixon.

Staff present: Alan R. Yuspeh, general counsel; Alan L. Chvotkin, counsel; Jonathan L. Etherton, professional staff member; and Marie Chaillet, staff assistant.

Also present: Henry D. Sokolski, and Bill Hunter, assistants to Senator Quayle; Alan Ptak, assistant to Senator Gramm; Edward McGaffigan, Jr., assistant to Senator Bingaman; and Milton D. Beach, assistant to Senator Glenn.

Also present: Bill Montalto, Small Business Committee.

OPENING STATEMENT BY SENATOR DAN QUAYLE, CHAIRMAN

Senator QUAYLE. The hearing will come to order. Today we will receive further testimony from outside witnesses on the implementation of the 1984 defense procurement legislation. Because of the large number of outside associations and individuals who wished to present their views, the subcommittee is pleased to devote a second hearing for this purpose.

This series of hearings has been extremely useful in surfacing preliminary concerns and problems with the implementation of the numerous procurement provisions enacted recently. At the same time, we are gaining a clearer understanding of the different varieties of defense procurement.

At the November 7 hearing, many of the witnesses felt that insufficient attention is being given to this fact as comprehensive and detailed regulations are proposed governing the procurement of weapon systems, spare parts or commercial products. It is still not clear, however, to what extent this problem is a result of the original legislation or the implementing regulations.

That is a key point. I hope our witnesses will be able to focus on and tell us which piece of legislation they would like to see modified or repealed. We have two panels today.

Senator Dixon has submitted a statement for the hearing record. Without objection, the statement will be inserted in the hearing record at this point.

[The prepared statement of Senator Alan J. Dixon follows:]

PREPARED STATEMENT BY SENATOR DIXON

Mr. Chairman, this hearing is the fourth you have chaired on the effect of the defense procurement reform legislation passed in the previous Congress. We have heard from the Defense Department, the military services and representatives of the major prime military contractors.

Today the subcommittee will be receiving testimony from witnesses representing small businesses. These men and women were the major force behind the two major bills we passed last year.

The legislation we passed last year did not embody all that the small business community wanted, but it was a very good piece of compromise legislation. It will increase competition in contracting throughout the Federal Government and, more specifically, in the Department of Defense.

I look forward to hearing from these individuals on how they feel the legislation is being implemented.

Thank you, Mr. Chairman.

Senator QUAYLE. Unfortunately we are voting this morning and I have to depart from here by noon. So, we are going to implement what we call our 5-minute rule for the witnesses. If you can summarize your testimony in 5 minutes or less, it will be greatly appreciated.

The full text of your testimony will be inserted in the record. I think that will leave us time for some questions and spontaneity.

I have a little light down there. The green light is "go," yellow light means you have 30 seconds. When the red light comes on, that means your time has expired. That does not mean you need to stop right on the red light. We are very accommodating here. If you can summarize 5 seconds after that red light, the chairman will be greatly indebted to you.

I will proceed according to my list. The first panel is Mr. Robert Clark, president and chief executive officer, the Goodyear Aerospace Corp., representing the National Security Industrial Association.

STATEMENT OF ROBERT W. CLARK, CHIEF EXECUTIVE OFFICER AND PRESIDENT, GOODYEAR AEROSPACE CORP. (REPRESENTING THE NATIONAL SECURITY INDUSTRIAL ASSOCIATION)

Mr. CLARK. Thank you, Mr. Chairman.

It is a pleasure to be here and involved in this proceeding. Recognizing the shortened time, I will do as you ask.

The statement which we have submitted in advance contains several examples of implementing problems relating to the legislative scenario. In the interest of your time, I am going to give a very foreshortened version and hopefully will be ready for questions.

First of all, I think it is important to submit for the record that we are an industry association concerned in many respects relative to our contribution to the ongoing defense procurement in several areas.

Our industry is making progress in its efforts to improve its business practices. We have achieved a greater sensitivity relating to industry-created problems and have increased our communications from senior management of our companies to all levels regarding corporate commitments to integrity.

We are witnessing a reemphasis and adoption of increasing numbers of corporate codes of conduct, internal compliance reviews and better training. We realize we share a burden along with Government to help resolve some of the perceived problems, that we have to look in the mirror before we ask for help.

We note in the testimony before your subcommittee last Thursday, November 7, other major defense-related associations testified on many matters which are of concern to us. I wish to highlight those because they are of concern:

The flood of legislation and its implementation;

The need to reduce the volume of regulations imposed on the process;

Micromanagement by both Congress and DOD;

Growth of congressional oversight committees and subcommittees;

The lack of strong direction and clear lines of acquisition authority in the Department of Defense;

The failure to adhere to the Federal acquisition or FAR system;

The need for more and earlier industry participation in developing policies and regulations;

The need to reverse the Government intrusion into corporate management decisionmaking responsibility;

We are fully accountable and wish to remain so;

The need to restore the authority and the accountability of the contracting officer; and

The adverse effect of the proliferation of audits.

We strongly agree with all these points that were presented to your committee. Rather than repeating the discussions here, I will focus on a couple of examples.

The Procurement Reform Act of 1982. In any discussion of legislation put in place to control the functions of the executive branch, consideration, we believe, must be given to both the law itself and to its requirements and the method and form by which it is implemented.

It is also well to remember that reform legislation, by and large, is reactionary legislation and, as such, involved both emotion and facts in arriving at the concept of what is needed in the way of public law to correct a perceived problem.

Such a situation exists in Public Law 98-525, a part of the fiscal 1985 Authorization Act. This public law resulted in the issuance of Federal Acquisition Circular 84-10 which was presented to the general public as a vehicle for implementation of that law together with other laws.

I would like at this time, Mr. Chairman, to discuss this law and its implementation in the Federal Acquisition Circular as published in the Federal Register.

There are three parts of the circular that have their origin in Public Law 98-525. One deals with planning for future competition—acquisition of technical data—another with integrity of unit prices, and the last with certification of commercial prices.

Unfortunately the language of the law was rather imprecise, but it was the law and it needed to be implemented. I will use this implementation process as a case study to highlight a significant problem in the congressional, executive branch, and industrial relationship.

The law calls for implementation within 180 days from the day of enactment on October 19, 1984. There was a significant impact on the way contractors would have to do business in the future. Because of the impreciseness of the language, it should have been necessary for those impacted most to have been involved in the development of implementing regulations.

Noting the orange light, let me offer this comment. We understand and believe in the implementation of law and some reform is necessary. We encourage that industry be allowed to be accountable as it should be for the results of this process.

We submit that micromanagement designed to solve small problems generally gets confused in its application across a broad spectrum in the system. We would encourage very careful reaction on the part of Congress in terms of the law they implement.

In the interest of time, I will conclude my oral remarks. I would encourage the subcommittee to read carefully the submittal we have made.

[The prepared statement of Mr. Clark follows:]

PREPARED STATEMENT OF ROBERT W. CLARK, CHAIRMAN, BOARD OF TRUSTEES, NATIONAL SECURITY INDUSTRIAL ASSOCIATION

Mr. Chairman, my name is Bob Clark. I am the president and chief executive officer of the Goodyear Aerospace Corp. and also chairman of the board of trustees of the National Security Industrial Association [NSIA]. I am pleased to appear before this subcommittee today, in response to your invitation, on behalf of NSIA. Our association has a broad membership of some 390 organizations including companies both large and small, prime contractors and subcontractors, from all segments of industry. It has served for 41 years as a major instrument of communication between Government and industry. While it does not advocate or lobby for the special interests of any trade or group, it is a representative of American industry which strives together with Government toward the ultimate goal of "a nation secure".

My remarks today will present for your consideration our views as to how certain legislation passed in 1984 has impacted the enormous and complex defense procurement system and how we expect the 1985 authorization and appropriation bills to further complicate the procurement process.

First of all, I want to assure this subcommittee that we are concerned that in many respects industry has been its own enemy in contributing to the ongoing defense procurement furor in several areas. We have been reluctant to refuse to bid on stupid contracts. We have sometimes accepted contracts that were unrealistically priced too low, contributing to later apparent "overruns." We have often accepted contracts for uneconomic quantities. We have accepted gold plated specifications. We have rigidly complied with mandated accounting principles even when the resultant prices bore little relationship to the intrinsic value of the item, and we have on occasion accepted terms and conditions and types of contracts that we should not accept.

We recognize a need for the industry which supports our defense efforts to be more responsible suppliers. We must not forget our responsibilities to the buyer, ourselves and most importantly the public.

Our industry is making progress in its efforts to improve its business practices. We have achieved a greater sensitivity to industry created problems and have increased communications from the senior management of our companies down to all levels regarding corporate commitments to integrity. We are witnessing a reemphasis and adoption of increasing numbers of corporate codes of conduct, internal compliance reviews and better training. Greater corporate self-discipline is required and it is forthcoming.

We have recommended that each company adopt a strong code of corporate conduct and review its policies and operating procedures to assure that its implementing actions will result in full compliance with Government regulations. Each company should also broaden its internal audit program to include in-house audits for self-policing purposes. Also we believe that industry should improve the training of its personnel in all areas of the defense procurement process including the nature of Government business as compared to private sector business.

So we in industry share the burden, along with Government, to help resolve many of the real and perceived problems which exist in the defense acquisition system.

I will now move to the area which your subcommittee is examining in these hearings.

We note that in testimony before your subcommittee last Thursday, November 7, other major defense-related associations testified on many matters which are also of deep concern to NSIA. Among these are:

The flood of legislation;

The need to reduce the volume of regulations;

Micro-management by both the Congress and the DOD;

The growth of congressional oversight committees and subcommittees

The lack of strong direction and clear lines of acquisition authoirty in DOD;

The failure to adhere to the Federal acquisition system (FAR);

The need for more and earlier industry participation in developing policies and regulations;

The need to reverse the Government instrusion into corporate management decisionmaking responsibility;

The need to restore the authority and accountability of the contracting officer; and

The adverse effects of the proliferation of audits.

We strongly agree with all of these points, and, rather then repeating those discussions here, I will today focus in some detail on some of the specific areas which we believe to be particularly significant.

Procurement Reform Act of 1984.—In any discussion of legislation put in place to control the functions of the executive branch, consideration must be given to both the law itself, and its requirements, and to the method and from by which it is implemented. It is also well to remember that "reform legislation" by and large is "reactionary legislation" and as such involves both emotion and facts in arriving at the concept of what is needed in the way of a public law to correct a perceived problem. Such a situation exists in Public Law 98-525, a part of the fiscal year 1985 authorization act.

This public law resulted in the issuance of Federal Acquisition Circular 84-10 which was presented to the general public as the vehicle for implementation of that law together with other laws.

I would like at this time, Mr. Chairman, to discuss this law and its implementation in the Federal Acquisition Circular as published in the Federal Register.

There are three parts of the circular that have their origin in P.L. 98-525. One deals with planning for future competition (acquisition of technical data), another with integrity of unit prices, and the last with certification of commercial pricing.

Unfortunately, the language of the law was rather imprecise, but it was the law and had to be implemented. I will use this implementation process as a case study to highlight a significant problem in the congressional, executive branch, and industry relationships.

The law called for implementation within 180 days from the day of enactment, October 19, 1984. There was a significant impact on the way contractors would have to do business in the future, and, because of the impreciseness of the language, it should have been necessary for those impacted most to have been involved in the development of implementing regulations.

There was no effort to consult with industry, even though other existing regulations call for public comment unless there is a justifiable reason for immediate implementation. Congress allowed ample time. However, the regulatory councils did not meet the congressionally imposed deadline. Some 3 months after that deadline, the Federal Acquisition Circular was published as a mandatory requirement with a request for after-the-fact comments to the council within 30 days.

Some Government agencies immediately issued orders saying the rule had retroactive application to the date that Congress had directed its publication. Thus began the confusion.

In addition to that issue, the councils determined that this was an opportunity to incorporate into the implementation of the law other requirements they felt would be nice to have . . . like extended data requirements and extensive audit requirements . . . far beyond anything industry had visualized from the law as enacted.

Because of the perceived overreaching and totally impractical—and in some instances—almost impossible requirements added to the statutory requirements, there was an instant uproar from industry . . . so much so that the councils held an unprecedented public hearing on September 10, at which many of the shortcomings in the Circular 84-10 were again brought to the attention of the councils. Previous input has been in writing.

As a result of this meeting industry was given to understand that immediate action would be taken to mitigate the requirements to the point that implementation would not be preceived as being as onerous as when initially issued.

In the meantime the implementing rules had been submitted to the Office of Management and Budget for review and approval before the information requirements set forth therein could be imposed. On September 25, 1985, the request was returned marked "not approved" because the practical utility of the reporting and record keeping requirements had not been shown.

As far as we know, the implementing agencies have ignored the findings of the OMB. We have seen no hold-up in the imposition of the requirement in contracting actions.

Mr. Chairman, I have purposely refrained from getting into the details of the over implementation of the law on the part of the Federal acquisition regulatory agencies. There is a compendium of discussions in the hands of the councils that can be made available to you upon request . . . or if you wish, we can obtain a number of the letters sent to the defense and civil agencies acquisition regulatory councils and submit them to you for the record. In any event, I believe it will suffice to say that what started out to ensure appropriate pricing has turned into an administrative nightmare of tremendous proportions. This process is repeated time after time with each new piece of legislation.

The Competition in Contracting Act of 1984.—Although this act was implemented 1 April 1985, we are not yet in a position to provide a comprehensive assessment of its effectivity and appropriate recommendations. We perceive that implementation is headed far beyond the intent of Congress. This could result in increased cost and manpower, schedule delay, increased introduction of foreign sources and voluminous, costly data production.

We continue to support the recognition in the Competition in Contracting Act that competitive negotiations may be as effective as sealed bidding as a technique for obtaining fair and reasonable prices. We strongly support competition when intelligently and judiciously applied.

The operative words are "intelligently and judiciously applied". Competition must be offered only to businesses qualified to compete which have a desire to compete. The forcing of a contract on unqualified bidders for the sole purpose of fulfilling a quota can destroy the procurement process as far as that procurement action is concerned with a resultant downgrading of quality, cost and schedule achievement.

We do not believe that meaningful competition can be achieved by creating competitors by openly making available all proprietary data to permit the creation of a facade of producibility on the part of newly created competitors.

Meaningful competition in highly technical programs, as opposed to commercially available products, exists only when two or more business entities, qualified to perform a task, freely and openly propose to fulfill a to-be-contracted-for function followed by explanatory meetings between the buyers and the sellers to achieve a complete understanding on the part of both participants as to what is needed to be bought and what is offered to fulfill that need.

When business opportunities exist which provide an appropriate return on resources applied, competitors are self-created. Competitors are most generally created well before a competition is held for proposals on a congressionally authorized program.

However, there are multitudes of items, usually of commercial nature, which can and should be advertised with minimum specifications, and procured through "open" competition.

Rights in technical data.—The Government for years has required that contractors provide technical data and drawings relating to deliverable items under contract. Contractors are entitled to limit the Government's "right to use" if the data pertains to effort done at private expense. In the last couple of years both the DOD and the Congress have addressed the need for the Government to acquire data in order to assure the Government's ability to complete future procurements. This concern was brought into focus by the DOD's initiative to increase competition in order to reduce spare parts prices, and in 1983 SECDEF directed military departments to negotiate contract data provisions which would reduce contractors' proprietary rights-in-data.

In 1984 an OSD data rights study group concluded that it was neither feasible nor necessary to obtain all technical data rights in order to accomplish competitive reprocurement of spare parts. Congress also actively pursued this issue and introduced numerous pieces of legislation reflecting their solutions for DOD's spare parts pricing problems. As an example, the Defense Procurement Reform Act requires DOD to issue regulations that govern contractors' and Government's rights in technical data.

However, in the interim of the last 2-3 years, industry has been forced to "negotiate" special Air Force and Navy clauses for data rights. Industry impatiently waited for the the new far data rights section release and when a draft was released with a 30 day review and comment period, industry reacted violently to the excessive overreach on the part of the DAR council, in terms of what Congress provided in statutory/legislative direction.

Credit is given to the DAR council, which upon understanding some of industry's concerns, issued an interim regulation and extended the comment period to 90 days. This, we hope, will provide sufficient time for industry and the DOD to provide final regulations that will recognize equity for both sides: Recognize the contractor's rights of privately developed data and provide a groundwork for encouraging insertion of private expense technology into DOD acquisition.

Warranties.—The statutory warranty provision (P.L. 98-525, 10 U.S.C. 2403) should be revised.

Product and specification performance warranty liability is being imposed on contractors, even though the designs and specifications are the Government's or are under Government control. The statute's legislative history (Senate Report 98-500; House Report 98-1080) states, inter alia, that performance guarantees could be narrowed where the contractor has not had full control over design and development. This legislative intent has been ignored.

Moreover, defense agencies often disclaim any responsibility for the suitability of Government-furnished specifications, designs and drawings. The warranty statute encourages Government carelessness in fulfilling its responsibility to furnish the contractor an adequate baseline for preparing bids.

Excessive warranty demands would be reduced if each warranty requirement were justified on the basis of a cost-benefit analysis, as the statute and legislative history anticipated. Defense agencies, however, have announced that they will refuse to recognize any warranty cost in a contractor's bid or will require contractors to submit contractual plans to assure no-cost performance warranties. Consequently, there is no effective cost/benefit safeguard against excessive warranty demands.

Congress should narrow the scope of the warranty statute by repealing the requirement for performance warranties, leaving intact the workmanship and material and the specification compliance warranties. This would conform more closely to commercial practices.

This year's legislative package contains major changes in the way the procurement process works both on the part of the Government and the contractor. Implementation will be dramatic and application on contracts can be chaotic. The first of these to be discussed is the extension of statutory determination of allowable costs.

Allowable cost issues.—There are too many initiatives and not enough planning and coordinated action in this area.

For example, last March the DOD initiated a requirement to certify that unallowable costs are excluded from indirect cost submissions to the Government. The requirement for exclusion of unallowable costs was already mandated in a congressionally approved cost accounting standard (CAS 405) effective April 1, 1974, which also included coverage on the appropriate accounting treatment for such costs. The DOD certification provided for perjury where noncompliance occurs, which was not provided for in the cost accounting standard. The current defense authorization bill applies the same requirement for certification already imposed by DOD, except that it adds specific penalties for noncompliance without defining the cost of those activities that are not allowable for Government contracting purposes.

The threat of penalties without clear definition is causing consternation, confusion and a substantial increase in administrative effort (and cost) to accomplish certification by responsible company officials.

There is already confusion and conflict between the cost principles and cost accounting standards. A recent armed services board of contracts appeals decision (the Boeing Co., ASBCA No. 28342) found that there was conflict between the cost principles and standards in accounting for pension costs and decided that cost accounting standards take priority over the far cost principles. Current actions by DOD to clarify the cost principles further exacerbates the conflicts that exist today.

DOD has been responsible for the cost principles for 35 years. The last time Congress became concerned with DOD's administration of the cost principles, a separate organization, the cost accounting standards board, was established by Congress to establish the accounting for contract cost. Responsibility for allowability issues remained with the DOD.

It would appear at this point that Congress should again consider whether DOD can do the job or whether an organization independent of DOD should be organized to take over full responsibility for both cost accounting standards and the cost principles. In this way we can avoid conflicts and have fair and reasonable regulations.

Work measurement standards.—We are greatly concerned with the potential imposition of work measurement standards on contracts as provided for in the current authorization bill. While work standards have been used in the defense industry for a number of years, the creation of work standards by statute raises the spectre of an administrative morass and a paperwork burden of inordinate proportion. It appears that there is no provision for the use of a cost-benefit analysis in its imposition nor for any determination of relief for type of contract or dollar value.

We anticipate significant cost increases in the cost of performance of those contracts on which it is imposed. We presume it will become the law and as such must be complied with.

Mr. Chairman, what I have conveyed to you represents a relatively small sample of what is going on in the Government procurement reactionary environment. Each instance enumerated represents the perception of a significant problem on the part of one or more Members of the Congress. The legislation enacted is that which is perceived as needed to correct a problem. Unfortunately, because of the complexity of the procurement process, little recognition can be given to the cause and effect of a particular piece of legislation until the act has been passed and implementation is begun. At that time, conflicts in efficiencies and downright impossibles emerge.

In 1970, the Commission on Government Procurement identified some 4,000 specific individual laws which impacted on procurement. While I am not aware of anyone currently counting, evidence assures us that the number is growing by leaps and bounds. I am advised that there are over 400 regulatory changes now backlogged in the OSD. Confusion in the defense acquisition process will continue to run rampant until the flow of new legislative and regulatory requirements is stemmed.

Mr. Chairman, I would like to conclude the NSIA statement by stating that we applaud your subcommittee for taking this time to conduct an oversight of the recent legislation. This is the appropriate role of the Congress.

We do not believe additional legislation is necessary at this time. We urge the subcommittee to issue a report which recommends to the full committee and to the Senate that additional procurement legislation be delayed until there has been ample time for the implementation of that which has already been enacted. As a more long range goal we believe the subcommittee should address the necessity for a more comprehensive review of the existing statutory basis for the acquisition process, with the objective of reducing the volume of applicable statutes and replacing them with a less detailed, more policy oriented, legislative approach.

We wish you great success in these hearings Mr. Chairman, and hope among the many achievements of this effort will be the following:

A marked lessening of the adversary relationship between the Government and industry.

A reduction of new procurement legislation to only that absolutely essential for defense operations.

A clear statement that the drive for more competition should not lose sight of the overriding need for quality, performance and reliability.

A clear statement that the drive for more competition should not lose sight of the overriding need for quality, preformance and reliability.

A reaffirmation of the predominant role of the contracting officer.

An indication by the Congress that excessive monitoring of the contractor's operations by the many agencies involved is counter-productive.

A return to the concept of reliance on "reasonableness" in determining allowable costs.

The need for clearer lines of accountability in the defense policy structure so industry will know "who is in charge."

A statement of the need for DOD application of more commercial practices and use of more commercial items and components.

A statement of concern by the Congress for a return to emphasis on protecting a viable industrial base.

Your hearings, Mr. Chairman, are very timely and your interest cannot but help to focus on the need to review the oustanding laws and streamline the entire process.

Thank you for this opportunity to discuss these items with you.

Senator **Quayle**. Thank you very much, Mr. Clark.

I think you are specific in some of your recommendations and that is precisely what we want.

The next is Mr. James Lightner, president and chairman of the Electrospace Systems, Inc., representing the American Electronics Association.

Mr. Lightner, you may proceed.

STATEMENT OF JAMES R. LIGHTNER, CHAIRMAN AND PRESIDENT, ELECTROSPACE SYSTEMS, INC. (REPRESENTING THE AMERICAN ELECTRONICS ASSOCIATION)

Mr. **Lightner**. Mr. Chairman, 95 percent of our business is done with various agencies and departments of the Department of Defense. Ninety percent of this business is done on a fixed-price basis won in competition.

Now, these are competitive procurements, but somehow the Government continually calls them negotiated contracts. It is my belief that it is the responsibility of Government and industry to maintain a strong defense at the lowest possible cost. More legislation and more regulation will not help us get this job done.

Government is literally strangling the defense industry with too much of this legislation and much too much regulation. Added regulations are driving our costs higher and higher and, frankly, I do not believe that these regulations are helping the product quality or making shorter delivery schedules or improving supportability in the field.

For example, recently one Government representative was forcing another costly regulation on one of our company officers. The representative acknowledged that the added documentation required was worthless, but if they did not force it on us, it would give us an unfair advantage on the competitors that already had yielded to the requirement.

In the early 1960's when McNamara first took office, I first started facing people who were assigned the responsibility to monitor and audit programs but who really had no idea what the program was all about; and this matter has continuously gotten worse ever since.

When it comes to competition, absolutely we should have competition wherever it is possible. You want to get as many qualified bidders that will possibly submit proposals. Competition helps and not only does it cost less, but it also gives the Government more than one idea on how to create the product or weapon system that will solve the problem.

However, if the DOD wants to encourage competition on the one hand, they should not turn around with the other hand and discourage competition by placing unrealistic limitations in bid and proposal policy which limits every company in their ability to compete. Also, unfortunately, with the encouragement for competition, many Government employees have now been assigned to the Competition Advocates Office and are creating additional paperwork and reporting requirements on the subcontracts that we have with our subcontractors.

Heaven only knows, our company already requires fierce competition on subs and we certainly do not need additional paperwork to do it. I also hate to see the unrealistic limitations on independent research and development work.

Moreover, the system that we have almost forces companies to waste money. I read about the $659 ashtrays and $3,000 coffeemakers and $414 wrenches. For the moment let us assume that each of these contractors is actually gouging the Government. If all the facts were known—I do not think they are really gouging the Government, but let us assume for the moment they are—in order to correct this gouging, consider not just taking away the contractors' profit on these items, but taking away all the profits on all defense contractors and see how much we can save.

In 1984 it is my understanding that the Government spent $146 billion in the DOD budget. I have seen the financial results of many defense contractors and I think a good profit average is 5 percent or maybe 5½ percent at the most. Five percent of $146 billion is $7.3 billion. The maximum we can save is $7.3 billion; but our target should be realizing savings in the $146 billion.

I will have to shorten my statement. As far as changing some special laws, we recommend, and it is in our testimony, that Congress exempt all competitive contracts from the laws that have been passed. We also recommend extending the public comment period on proposed isolations to allow greater industry participation prior to using the regulations.

[The prepared statement of Mr. Lightner follows:]

PREPARED STATEMENT OF JAMES R. LIGHTNER, CHAIRMAN AND PRESIDENT OF ELECTROSPACE SYSTEMS, INC., ON BEHALF OF THE AMERICAN ELECTRONICS ASSOCIATION

Mr Chairman, it is an honor to appear before your subcommittee today to testify about the effects of recent procurement reform legislation. My name is James R. Lightner, and I am Chairman and President of Electrospace Systems, Inc. of Richardson, Texas. Electrospace Systems, Inc. employs over 1,400 employees. The nature of our business is designing, manufacturing and installing electronic equipment and systems primarily for the Department of Defense. This fiscal year our revenues will be in the order of $140 million of which 95 percent is with various agencies and departments of the Department of Defense. Ninety percent of our defense business is fixed price competitive.

I am appearing before you today on behalf of the American Electronics Association. AEA is the largest trade association of this nation's largest manufacturing industry. AEA represents over 2,800 high technology electronics manufacturers nationwide. Over 70 percent of our members are small companies, employing fewer than 250 employees. The majority of those companies performing government contracts sell off-the-shelf commercial technology to the federal government--if they perform government contracts at all. Together, AEA member companies account for 63 percent of the worldwide sales of the U.S.-based electronics industries. According to Department of Commerce statistics, twenty percent of all U.S. electronics industry sales were made to the federal government in 1983; 16.6 percent were made to the Department of Defense.

AEA believes that by applying a variety of restrictions, regulations, and laws to situations where they don't belong--competivive acquisitions--the intent of Congress to differentiate between competitive and other than competitive situations is not being realized. As a result, contracts are being subjected to unnecessary administrative costs and delays; and contractors are discouraged from performing competitive federal contracts. In the end, the government and taxpayer will lose the advantages inherent in competition: high quality products at the lowest possible price.

PART I: BACKGROUND

We firmly believe that the intent of both government and industry is to get the best overall value for the dollar in acquiring goods and services to fulfill our national defense needs. The best value means not only the lowest possible price, but the best quality and most technologically sound product over the life cycle of that product.

But the procurement system today is badly clogged as both the contractor and government procurement community struggle to understand and implement the massive changes to the system ordered in 1984. In attempting to effect an environment wherein the best value of goods and services procured can be realized, the 98th Congress enacted at least four major procurement reform bills (PL 98-72, PL 98-369, PL 98-525, PL 98-577). Additionally, the government-wide Federal Acquisition Regulation (FAR) was amended 14 times since it was issued in April of 1984; the Defense FAR Supplement (DFARS) was changed or amended 11 times; and scores of directives from the various military services and the Office of the Secretary of Defense (OSD) were issued. There is no end in sight. As a report by the Congressional Research Service on PL 98-369, the Competition in Contracting Act (CICA) noted, 1984 "registered unmistakable readings on the procurement Richter scale."

It is too early to determine precisely the effect of many of these changes. CICA, for instance, became effective only this Spring.

1984 changes to the rights in technical data provisions--an extremely sensitive area for most contractors, especially commercial companies--became effective on October 19; and these changes are only "interim" regulations.

It is not too early, however, to comment on the cumulative effect of these changes on the defense acquisition environment. **The purpose of this testimony is to examine the current procurement environment and to determine whether the intent of Congress and industry to get the best value for the procurement dollar is being realized.**

This testimony will review the recent procurement reform statutes and their implementation as well as a variety of other environmental factors which impede efforts to encourage competition and to acquire the best goods and services at the best value.

PART II: THE LAW AND ITS IMPLEMENTATION

AEA Concerns with 1984 Procurement Reform Statutes

The most important procurement reform statute enacted by the 98th Congress was the Competition in Contracting Act. AEA supports the concept of separating competitive procurement from "other than" competitive procurement. In this manner, Congress realized that in most situations, marketplace incentives should play the dominant role in determining how the government acquires goods and services.

AEA is concerned, however, that certain provisions of recently enacted law will discourage, rather than encourage competition. In short, we believe that **restrictions designed to regulate "other than" competitive situations are being applied inappropriately to competitive acquisitions.** Thus, while the government says it wants to rely more on marketplace incentives in acquisition policy, its actions speak differently.

Life-Cycle Costs not Adequately Addressed

CICA recognizes that there are situations where competition is not necessarily appropriate. For example, by making "other than" competitive contracts virtually impossible, contracts for reprocurements are being competed after an initial contract award to the lowest bidder. It is highly doubtful that recompeting these contracts saves anyone any money. Bid preparation and other activities associated with competing for a contract even before it is awarded costs both the government and contractors money. Further, the contractor bases his costs of production on life-cycle costs. If the contractor had to assume another competition of the same contract in two or three years, he would have to build into his contract the costs of gearing up for production over a shorter period. In short, the government saves no money, and likely increases its costs under such circumstances.

Cost and Pricing Certification Threshold Adds Unneeded Costs

CICA lowered the Truth in Negotiations Act cost and pricing certification threshold on defense contracts from $500,000 to $100,000. While the government always had the authority to require certification below $500,000, requiring by statute certification for any contract over $100,000 has added tremendous administrative time and expense to the procurement process even in competitive situations. The $100,000 threshold was established in 1962; in current dollars accounting for the effects of inflation over the last 23 years, , the equivalent 1962 threshold would be about $500,000. Further, according to DoD tesitmony before this Committee during consideration of CICA, 92 percent of DoD procurement expenditures (FYs 82 and 83) involved contracts over $500,000; only eight percent fall under $500,000. Assuming that only a fraction of these latter contracts involve questionable prices for which certification may be justified, CICA imposes a considerable cost burden on contractors for little reason. This cost ultimately is borne by the taxpayer.

Warranties Provision Needs Improvement

As AEA has testified before this Committee in the past, we still question the reasonableness of requiring performance warranties on products not designed or manufactured by the contractor. Contractors are willing to provide warranties for products over which they exercise design and manufacture control. Requiring them to guarantee performance of a product which they did not design or manufacture, especially if such a product meets government-required specifications, merely discourages contractors from competing for contracts.

Data Rights Language Too Ambiguous

AEA's concerns about the protection of proprietary, commercial technical data are well known. While PL 98-525 directs DoD to "consider" data developed at private expense in drafting regulations, AEA believes that DoD should be prohibited from acquiring such data. The mere threat of losing commercial data to the government dissuades would-be contractors from entering into government contracts. Existing regulations clearly recognize commerciality and provide the basis for preventing abuse of such an exemption.

Section 8(a) Set Asides Open to Abuse

CICA also exempts from competition all Sec. 8(a) minority small business set aside contracts. AEA members note that this exemption is being abused. For example, it is being implemented in such a way as to preclude even other 8(a) firms from competing for the same contract. Furthermore, the exception is being used to direct awards to incumbent contractors without going through the competitive process. 8(a) firms are awarded contracts, without competition, and directed to subcontract 50 percent of the contract to the former (incumbent) prime contractor. The prime, meanwhile, is required to "gear up" the 8(a) firm to a point where it eventually may take over the entire contract, with or without "graduating" from 8(a) status. The prime, in effect, has been required to pay another firm to take away its contract, without the contract ever having been subjected to competition.

1984 Procurement Reforms Not Being Correctly Implemented

While AEA maintains certain concerns about the statutes, as mentioned above, we believe that both the letter and intent of Congressional procurement reform efforts are not being implemented correctly. Later in this testimony, we will discuss other factors not related directly to laws enacted during the 98th Congress which further impede competition and erode marketplace incentives in the procurement environment.

Public Comment Requirement Ignored

In an effort to control the issuance of agency regulations and to increase oversight and consideration of regulations prior to their final promulgation, the Competition in Contracting Act (CICA) requires a 30-day public review period during which parties affected by a proposed regulation may comment on the proposals. This requirement is being ignored regularly.

For example, in implementing CICA itself--an effort which amended over one-third of the newly issued Federal Acquisition Regulations--industry was given a five-day (later extended to nine day) comment period. We recognize that this abbreviated comment period was necessary to implement CICA by its effective date. Nevertheless, it is ironic that the first implementing regulation under the new law "required" a deviation from that law.

Other examples of DoD disregard of the public comment requirement abound. Earlier this year, Secretary of Defense Weinberger issued an order requiring that contractors certify all overhead expenses. The legality of the certificate requirement was questionable at best. As written, it was impossible to implement. In any event, it was issued as effective immediately, without public comment.

Again, this Summer, DoD issued without warning or comment a directive requiring across the board reductions in industrial security clearances, without regard to disproportionate burdens this requirement placed on small and/or growing operations.

Another example is Federal Acquisition Circular (FAC) 84-10, which among other things would require contractors to certify the price they offer the government on any product is the lowest of any offered to anyone in the last 60 days. Not only does this requirement represent a tremendous increase in administrative time and expense for contractors, it is unnecessary in situations involving competitive, commercial contractors; and it is probably impossible to comply with, especially for large commercial contractors who have hundreds or thousands of products being sold daily to customers around the world. Again, FAC 84-10 was issued without public comment, and made effective immediately. (Issuance of the certificate was denied by OMB; but DoD is seeking reissuance of a slightly modified version.)

The Navy recently issued a directive severely limiting per diem allowances associated with Navy contracts. This policy not only deviates from DoD policy and the FAR, (the General Services Administration recently testified that government per diem allowances should be increased) but was issued as effective immediately, without public comment.)

Finally, the public comment period is being ignored with the promulgation of "interim" and "interim final" regulations which are being issued as effective immediately. Not only does the use of such procedures circumvent the public comment period requirement, but it causes tremendous strains on contractors (not to mention government contracting personnel) who must keep up with such regulations which are only to be changed again at some future date.

Economic Order Quantities, Multiyear Procurement

Section 1202(3) of PL 98-525 states that "the Secretary of Defense should make every effort to reform procurement practices relating to replenishment spare parts...Specifically, [he] should...direct that replenishment spare parts be acquired in economic order quantities and on a multiyear basis..." DoD is not complying with this provision. Spare parts still are being ordered in uneconomic quantities; and life-cycle costs requiring multiyear planning rarely are being considered. The likelihood of future spare parts scandals therefore will not be diminished.

Regulations Are Expanded Beyond Intent of Law

Data Rights

PL 98-525 also contains several provisions regarding the rights of the government to certain technical data relating to products procured by the government. These provisions state that in drafting implementing regulations, the Secretary shall consider "whether the technical data was developed...exclusively at private expense; or in part with Federal funds and in part at private expense." In issuing proposed implementing regulations (since withdrawn), DoD completely ignored these vital distinctions.

Warranties

Both the FY 84 and FY 85 Defense Authorizations Acts contain provisions requiring contractors to provide warranties on major weapon systems sold to the government. While PL 98-525 clarified that warranties are not appropriate until a product reaches full-scale development, DoD nonetheless has insisted upon warranties on weapon systems which are not in full scale development. There also is a growing perception that DoD is requiring "general standards," contrary to what we believe is the intent of the law, such as (i) a warranty probably should be no more than "x" percent of the contract price; (ii) the warranty period for all items should be "x"; (iii) the turnaround time for all items, complex or simple, must be "x" regardless of the type of failures; and (iv) a warranty ceiling should be at least greater than the contract profit and not less than "x" times the warranty price. The effect of these requirements is to deprive contractors and contracting officers the flexibility necessary to negotiate warranties which reflect the nature of the system being procured. Without such flexibility, contractors will be reluctant in certain circumstances to provide their products to the government.

Commercial Pricing Certification

In this new procurement environment, overregulation has become commonplace. As mentioned above, certifications that the government should receive as low a price for spare parts as the lowest commercial price have been expanded in FAC 84-10 to include prices of all kinds of products, rather than just spare parts, and to include prices to government agencies as well as commercial suppliers. This expansion of statutory intent fails to recognize the costly administrative burden placed on a sequentialized volume supplier with diversified channels of distribution. Similarly, legislation intended to ensure that prices of spare parts are not made unreasonable because of unbalanced allocation of overhead has been expanded to cover all products with no exemption for standard commercial products.

DoD Regulations Ignore Statutory Definitions

Finally, DoD regularly fails to use statutory or FAR definitions and terms in issuing its own regulations. For example, proposed DFARS regulations (since withdrawn) implementing the data rights provisions of PL 98-525 failed to use statutory definitions of "technical data", "item", "item of supply" or "supplies" as defined in Sec. 102, PL 98-577.

I should note that while some of the above instances of ignoring the letter and/or intent of law have been (temporarily) "resolved" by withdrawal of proposed regulations or modification thereof, these examples still illustrate a "regulate first; read the law second" kind of implementing procedure. This is no way to foster an environment conducive to competitive marketplace practices.

PART III: OTHER FACTORS AFFECTING THE ACQUISITION PROCESS

In addition to the recent procurement reform statutes and implementing regulations, several other factors relating to the acquisition process directly impede greater competition and participation in federal procurement, contrary to the intent of government and industry alike.

Overreaction by Congress, the Administration, Media

The greatest single "environmental" factor causing disservice to efforts to improve the procurement process is overreaction by the Administration, Congress, federal agencies and the national news media to instances to fraud, waste and abuse in the procurement community. This is not to say that fraud, waste and abuse do not exist. Serious efforts should be made to minimize what's wrong with the acquisition process. On the other hand, serious efforts also must be made to maximize what's right with the process.

It should be noted, for example, that hundreds of thousands of procurement actions are completed each year. In FY 84, DoD alone procured goods and services worth over $146 billion--an almost incomprehensible amount of money. Rarely do we read that over 80,000 hammers were procured last year at a cost of about $7 apiece; or that the so-called overpriced $659 custom ashtray cost the Navy $900 to produce in-house; or that a $3,046 coffee maker cost commercial airlines $3,107; or that a $414 customized wrench was replaced by a less expensive one which damaged firing bolts on Navy ejection seats at a replacement cost of $218 each, far exceeding the cost of the original wrench. How much policy is being made based on inaccurate or misleading information?

Overreaction in the press and by policy makers in turn creates an environment which is unnecessarily restrictive. The widespread but mistaken perception that the acquisition process is completely broken down has created an atmosphere in which timely acquisition of products has become secondary to making the acquisition process perfect. Achieving the lowest possible price on any item has been substituted for efforts to achieve the best value of defense goods and services.

Circumvention of Competitive Process

Ironically, efforts to perfect the process in many instances actually are discouraging greater use of competition and commercial product acquisition. This is because **all acquisitions regardless to the presence of competition or commerciality are being subjected to the same procedural restrictions designed or intended to apply to non-competitive situations.** While CICA may have recognized the distinction between competitive and "other than" competitive situations, in the current procurement environment, this distinction is not made. Thus, competitive contracts are subjected to the same audit requirements, certifications, paperwork requirements, etc. as if they were sole source contracts. The government appears unwilling to accept competition even when it is present.

For example, in situations where DoD admits full and open competition exists with two or more qualified bidders competing for a contract, it requires cost and pricing data, on the basis that there may not be "adequate price competition." This places commercial suppliers in the position of being unable to comply, and therefore to compete. As a further case in point, form DD-7, which used to exempt commercial contractors from cost and pricing certification requirements has been "amended" to require certification of lowest price.

In short, by treating "competitive" contracts as "negotiated" contracts, DoD effectively circumvents the use of competitive procedures; and thereby is able to impose requirements usually associated with sole source or other non-competitive contracts in otherwise competitive situations.

In its zeal to achieve the lowest possible price for products, DoD is paying less attention to quality, technical and technological superiority, long-term ability to perform a contract, life-cycle costs and other factors which affect the overall value of a contract. For instance, our memebers report that "buy-ins" are being accepted and even encouraged--virtually ensuring future cost overruns. Additionally, RFPs and evaluations too often give minimal weight to quality. During the best and final offer (BAFO) process of contract negotiations, technical data is shared with competitors which tends to "level" the competitive edge of offerors and reduce their incentives for competing. In other situations, the advantages of competition are circumvented by awards to incumbents based on "technical merits" when price or other factors may have meant the incumbent's loss of the contract. In short, all of the factors which make competition a procurement objective--price, quality, efficiency, technological development, etc.--are not being allowed to prevail.

Furthermore, procedures already are in place which encourage federal agency acquisition of commercial products without having to go through more complex and costly administrative procedures associated with sole source or other than competitive situations. These procedures, the multiple award schedule (MAS), are being ignored by DoD.

Restrictions Increase As They Flow Down Procurement Chain

Another factor impeding the growth of competitive contracts is a phenomenon in which statutory or regulatory requirements are "flowed-down" from the government to the prime contractor and on to second, third and lower-tier subcontractors. Even though legislation, for example, may not include a flow down requirement, implementing regulations and prime contractors will pass through these requirements in an effort to minimize their own risk or exposure. Additionally, each flow-down requirement gets stronger as it is passed down the procurement process. This, too, is done to minimize the risk to the procuring contractor or agency. Thus, warranties requirements, for example, which apply to "major weapon systems" are being imposed on subcontractors of components. Similarly, data rights restrictions, overhead certificates, etc., are applied to situations where they are neither necessary nor contemplated by Congress. It is unfortunate that the most restrictive requirements end up being applied at the end of the procurement chain: the small, usually entirely commercial contractor furthest removed from the prime contract and least capable or willing to put up with government regulation. Obviously, this phenomenon further dilutes the intent of Congress to distinguish between competitive and "other than" competitive situations.

Changing and Inconsistent Regulations

Instability and inconsistency are among the most destructive forces to deal with for the business community. These two forces, however, are running rampant in the procurement environment. A few examples will illustrate this point. In September of 1984, the Navy issued a technical data rights policy which, efforts in Congress and an OSD study notwithstanding, considered "standard commercial products" only as those "manufactured by more than one source," regardless of how the product was developed or funded. Furthermore, In 1983 and twice in 1984, the Air Force issued data rights policies and revisions thereof.

Another frequent example of instability which makes contracting with the federal government costly and cumbersome is the use of "interim" and "interim final" regulations, as mentioned above. These regulations serve as more or less temporary regulations--only to be changed again at some undetermined future date.

Not only do the Services contradict themselves, but they deviate regularly from OSD policy and from the FAR, supposedly designed to create uniform government-wide acquisition procedures. The Navy, for example, has issued a policy on relief of subcontractors from liability for loss or damage to government property which is a direct contradiction of FAR 45.103 dealing with the same issue. Again, the Navy's per diem policy (since withdrawn) deviated from the FAR, an OSD directive, and CICA.

Perhaps the most frequent example of inconsistency of procurement policies can be found in the use of agency supplements to the FAR. The Defense Federal Acquisition Regulation Supplement (DFARS) is virtually a second FAR. Contractors who happen to sell goods and services to DoD and other federal agencies need to play by two sets of rules. There is no need in many if not most instances for the DoD to establish separate procedures, especially when dealing with competitive and commercial contracts. The proposed DFARS coverage of data rights serves as an example. Both the FAR Secretariat and DoD issued entirely different implementing regulations which apply to practically identical statutory language. Furthermore, DoD rarely if ever seeks FAR Secretariat review of its deviations from the FAR, as required by law, FAR 1.304 to control and limit the issuance of agency regulations, OMB Bulletin 85-7, and Executive Orders 12291 and 12498.

Congress itself is responsible for internal contradictions. Legislation (PL 98-620) reported out of the Senate Judiciary Committee last year, for instance, grants to federal contractors title to data developed even exclusively with federal funds. While this provision was subsequently limited only to small businesses, universities and non-profit organizations, it still is directly contrary to the Armed Services Committees' approach to technical data rights. This year there is the specter of significant contradictions between procurement reform language contained in authorizing and appropriating legislation.

Merely "keeping up" with these changing and differing regulations, not to mention complying with them, requires time and expense which is inconsistent with and counterproductive to competition.

Disregard for Small Business and Paperwork Impact

Another law (PL 96-354) frequently disregarded in the promulgation of acquisition regulations involves providing small business and paperwork "impact statements." In practice, the regulatory process gives these requirements scant attention. For example, the proposed DFARS regulation implementing data rights stated:

> DFARS Subpart 227.4 appears not to have a significant economic impact on a substantial number of small entities [and] imposes no new requirements which would require such entities to change their business practices, incur additional costs or otherwise affect their competitive position.

Although the proposed DFARS has subsequently been withdrawn, this type of language is inserted perfunctorily in promulgating regulations.

Overspecification

Overspecification of products is another problem which causes inefficient and costly acquisitions. While efforts currently are underway to reduce overspecification they appear piecemeal. The mere existence of detailed specifications in many instances discourages competition and the acquisition of commercial products.

Inadequate Personnel Training and Management

Several issues relating to training, management and responsibilities of procurement personnel also directly affect the procurement process. Most importantly, the fading distinction between the responsibilities of contracting officers versus auditors (with increased authority being given to the latter) not only is causing confusion in the contracting community but is fostering an adversarial relationship between parties negotiating contracts. Whereas audit reports used to be elements in certain types of contract negotiations, they now are being used to form the basis of contract negotiating strategy. Contracting officers, whose responsibility is to oversee all of the elements of a contract, are reluctant to take independent action. Auditors, on the other hand, whose sole responsibility is to review (not set) cost and pricing data, effectively are controlling the entire contract negotiations.

Adding to this problem is the fact that the technical training and competence especially of auditors but also of contracting officers vary significantly between agencies. Thus, while a company may be conducting negotiations professionally and efficiently with one agency, it may be bogged down on a similar contract with a different agency or different negotiating team.

Redundant, Unnecessary Audits

AEA testified before this subcommittee earlier this year on the lack of coordination between agencies with various audit and review authority. While the Inspector General attempted to explain that there is a difference between "audits," "reviews," and "investigations," a contractor understantably sees no distinction. The Inspector General (IG), Defense Contract Audit Agency (DCAA), and Defense Contract Administrative Service (DCAS), as well as the DCAS Regional (DCASR) and DCAS Management Area (DCASMA) offices all conduct their own "activities," regardless of what they officially are called. The result of these overlapping audits is redundancy, costing time and expense for the government and contractors and yielding negligible benefit to the government.

Unwarranted Government Claims to Commercial, Proprietary Data

In a related development, the government increasingly is asserting a "right" to to gain access to more and more data which is less and less directly related to a government contract. Internal audit reports, Board of Directors minutes, corporate planning documents and other records which may be subpoenaed justifiably in criminal investigations are being sought increasingly in the context of "normal" audits. In the case of a large, and/or commercial company which happens also to perform government contracts, this assertion not only is unwarranted, but is perceived as a direct threat to its commercial competitiveness. The threat of surrendering commercial data unrelated to a government contract, much like the threat represented by granting to the government rights to proprietary technical data, strikes at the very foundation of free enterprise. This threat is eroding our defense industrial base by discouraging companies' participation in the federal market.

Harassment

Finally, another common and unfortunately growing pheonomenon in the procurement process is the government's liberal use of stop-payments, contract terminations, criminal penalties, and other forms of harassment to force contractors to yield to various government requirements, regardless of the reasonableness of such requirements. The overhead certificate issued by the Secretary of Defense, discussed earlier, not only carried with it a criminal penalty of perjury if actual overhead expenses were found--for whatever reason--different than certified expenses, but DoD personnel were instructed to withhold contract payments on existing contracts if contractors did not sign the certificate. Similarly, the Navy ordered payments to be stopped on any contract not complying with its per diem policy. At least one AEA member company has had its shipments stopped not because of any problem with the product, but because the company had not "properly" followed certain procedures. Rather than maintaining an orderly--and consequently cost-efficient--production rate, the contracting officer in effect obstructed the timely acquisition of goods for reasons unrelated to the product's quality or value.

PART IV: EFFECTS OF THE CURRENT PROCUREMENT ENVIRONMENT

So far, we have discussed our various concerns not only with 1984 procurement reform statutes and their implementation, but with other elements of the acquisition process. Generally speaking, the cumulative effect of these concerns is to discourage contractors, especially those companies which have a choice of entering into government contracts or not, from performing government contracts.

Lead Time Increased: Readiness Reduced

One of the most measurable effects of the various conflicting and inconsistent procedural requirements imposed on contractors is the increase in lead time necessary to perform federal contracts. As graphically illustrated in the attachment to this testimony, a weighted average of administrative lead times (ALT) for Air Force Logistics Command contracts, for example, virtually doubled from FY 83 to FY 85.

Increased lead time in the timely acquisition of important goods and services for the national defense directly threatens our defense readiness.

The additional time it now takes to bring an item into production is causing contractors to begin contract performance increasingly frequently without a definitized contract. Prime contractors are being asked to sign "letter contracts" and primes are asking their subcontractors to do the same. This is because government agencies and contractors have production schedules, budgets and other deadlines which are being delayed due to the increased administrative burdens caused by new laws and regulations. We now are seeing both primes and subs refusing to enter into such letter contracts, causing more lead time delays. Not only is this trend further eroding defense readiness, but it puts both the government and contractors at additional risk, especially in cost reimbursement situations which are appropriate under letter contracts.

Unnecessary Restrictions Add to Contract Costs

Increased legal and administrative time and expenses related to complying with additional audit, certification and general procedural requirements not only reduce contract efficiency but increase contractors' and ultimately the government's procurement costs. As a case in point, one AEA member company derives 50 percent of its sales from the commercial marketplace, and the other 50 percent from sales to various government agencies. Its administrative staff for government contracts (kept separate from its commercial administrative staff) is twice the size of the commercial counterpart.

Unequal "Partners" to Negotiations

Overreaction to cases of waste, fraud and abuse as represented by efforts to make the system perfect have led to the loss of necessary flexibility in the negotiating process. If parties do not enter into negotiations as equals, capable of reaching mutually beneficial agreements, the negotiation process breaks down. Stop payments, increased use of criminal penalties and investigations, and other forms of harassment cause a lack of cooperation and trust between contracting parties. Again, the first parties to break off negotiations under such circumstances will be those who have a choice between entering into government contracts or not.

Innovation Is Discouraged

Increased assertions aimed at gaining access to commerical and/or proprietary information, as well as other efforts perceived by contractors as potentially compromising competitive information are leading to less risk-taking both by contractors and contracting officers. Contractors will be less willing to offer the government their best, most technologically competitive products for fear of losing their edge to competitors. Contracting officers, on the other hand, are less willing to accept these competitive risks for fear of running afowl of any number of procedural or political barriers.

Threat to the Industrial Base

Ironically, in the zeal to increase competition and improve the acquisition process, the current environment actually will reduce the defense industrial base if it continues on the present course. Consequently, loss of competition and increased procurement costs--exactly the opposite of what Congress and industry want--will be the end result if the acquisition process fails to recognize the importance of stability, flexibility and efficiencies inherent in commercial competition.

PART V: RECOMMENDATIONS

If this testimony serves any purpose at all, it is to demonstrate the massive complexity and interrelationships in the federal acquisition environment. Attempts to put out "fires" in one place are futile if these relationships are not fully addressed.

The Competition in Contracting Act distinguishes between competitive and other than competitive situations. But if the intention of Congress is to improve the value of goods and services procured by the federal government by relying to the greatest possible extent on competitive marketplace incentives--and we believe it is--then procurement policies should allow these incentives to work. This involves a certain amount of risk by the government; but if a contractor has demonstrated its ability to survive the rigors of competition, the government has little to lose. Therefore, **laws and regulations intended to control contracts in other than competitive situations simply should not apply to competitive situations.**

Policies should recognize all of the factors involved in the acquisition process, not just pricing, in devising means to improve federal procurement. It is interesting to note in this regard that the President's Commission on Defense Management is studying not only the acquisition process itself, but DoD organization and structure, career management (career development patterns and training) as well as overall defense missions and the ability to carry them out efficiently and effectively.

Similar recent studies, including an October 16 report by the Senate Armed Services Committee staff, an October 9 testimony by the Congressional Research Service before the House Armed Services Committee, findings of the American Bar Association in July, and a February report of the Georgetown University Center on Strategic and International Studies all reach similar conclusions: while attempts to reduce certain costs and prices will yield some benefits, **far more can be gained by better planning over a product's life cycle, greater stability in procurement programs and budgets, and greater emphasis on natural market incentives.**

In this regard, greater attention must be focused on multiyear procurement planning and budgeting. One AEA member company recently was asked to provide a 20 year life-cycle plan to a Japanese company to support the acquisition of one of its products. American contractors are lucky if they are asked to provide 20 month plans. By better planning and budgeting for the life of a product, contractors will be able to develop the most efficient production rates to account for economies of scale. Similarly, this will enable them to minimize life cycle unit costs, saving the government and contractor time and money.

Another marketplace incentive which should be encouraged, rather than discouraged, is **allowing contractors to increase profit by reducing costs.** Competition, if allowed to prevail, will ensure that profits are not "excessive". To limit profits in competitive situations by regulation or statute fails to recognize the value of competition and directly contradicts any effort to encourage it.

The **training and professionalism of contracting personnel must be improved and made consistent throughout the federal government.** The responsibilities of various parties to contract negotiations, furthermore, must be clearly delineated and applied consistently.

The **acquisition policies of Congress, the Pentagon and its military services, and all federal agencies must be coordinated, and discrepancies held to an absolute minimum.** In this regard, the authority of the Office of Federal Procurement Policy (OFPP) to coordinate government-wide acquisition policy should be reaffirmed.

Similarily, **audits and reviews by various offices and/or agencies must be limited and coordinated.**

Finally, and perhaps most importantly, **Congress, the Administration and federal agencies, and industry must increase their lines of communication.** In the current procurement environment, the last parties whose advice is sought (if at all) by regulators are those being regulated. Too many recent statutory provisions have been enacted or almost enacted without sufficient or even any hearings. Further, federal law prohibits the effective participation of industry in the regulatory process. **A substantial amount of regulatory time and expense by both the government and contractors,** as evidenced by the withdrawal or "interim" issuance of several recent regulations, **could be saved if "industry" were given a greater voice prior to the promulgation of regulations.**

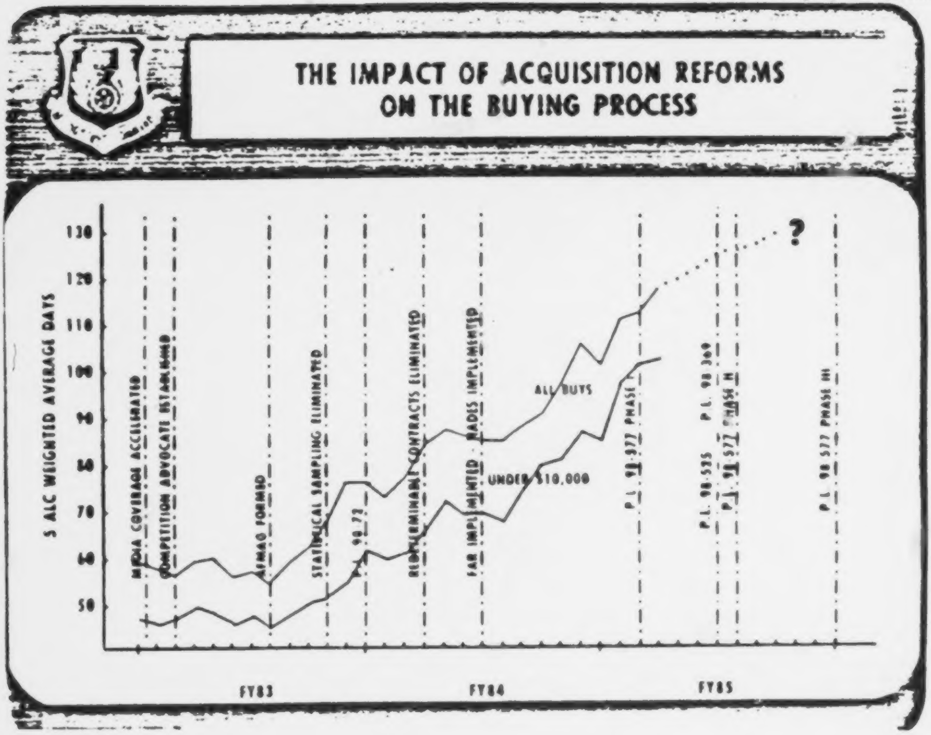
CICA's 30-day public comment period requirement should be extended to 90 days; and exceptions should be expressly prohibited except in extremely limited emergency circumstances. General Motors Corporation, which procured over $7 billion of computer products and services last year, developed its manufacturing automation protocol (MAP), now an industry standard for factory automation, by working as a customer together with its suppliers using only form, fit and function criteria. Both GM and its suppliers appear to be satisfied with this arrangement. Not only does this example argue against overspecification, but it argues for an environment in which the customer and its suppliers together develop the best possible acquisition process.

PART VI: CONCLUSION

In conclusion, Congress should focus not on procedure, but on defense missions and fostering an environment conducive to achieving them. Rather than looking at how each procurement dollar is spent, Congress should be concerned with how all defense dollars are spent.

Mr. Chairman, the American Electronics Association is honored to have this opportunity to comment on our nation's federal acquisition policies. Both the Association and its members are available at any time to discuss our positions in greater detail.

Source: Department of Defense
Air Force Logistics Command



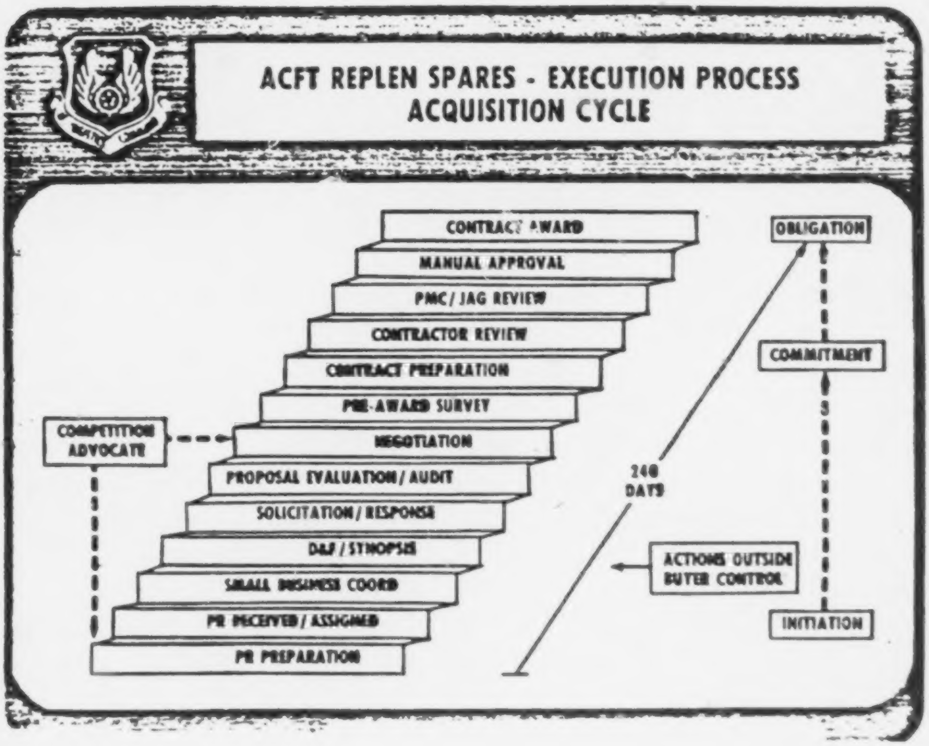
1535.7

Source: Department of Defense

ADMINISTRATIVE LEADTIME

	MID FY 83	SEP 84
SMALL PURCHASES	47	84
NEGOTIATED OVER S6M	167	230

Source: Department of Defense



ACFT REPLEN SPARES - EXECUTION PROCESS
ACQUISITION CYCLE

CONTRACT AWARD
MANUAL APPROVAL
PMC/JAG REVIEW
CONTRACTOR REVIEW
CONTRACT PREPARATION
PRE-AWARD SURVEY
NEGOTIATION
PROPOSAL EVALUATION/AUDIT
SOLICITATION/RESPONSE
D&F/SYNOPSIS
SMALL BUSINESS COORD
PR RECEIVED/ASSIGNED
PR PREPARATION

COMPETITION ADVOCATE

240 DAYS

OBLIGATION
COMMITMENT
INITIATION

ACTIONS OUTSIDE BUYER CONTROL

Source: Department of Defense 1535.8

WHERE DID ALT INCREASE

- PROPOSAL TIME (45 TO 60 DAYS)
- AUDIT/FIELD REVIEW (45 TO 78 DAYS)
- NEGOTIATIONS

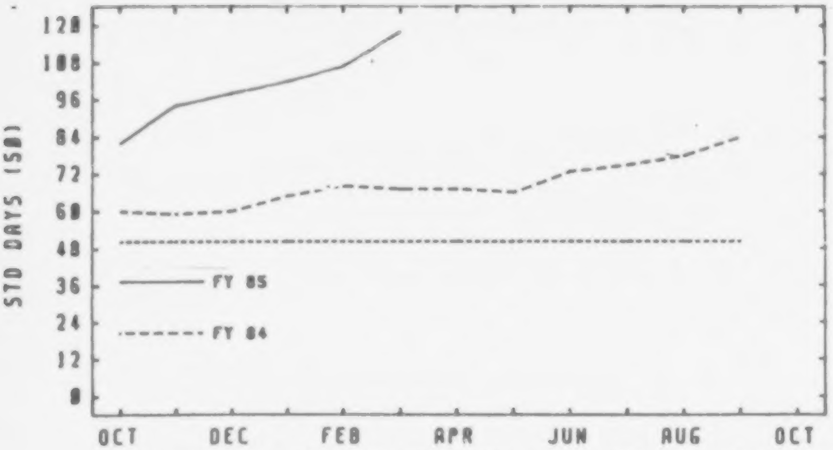
Source: Department of Defense 1535-2

CAUSES OF ALT INCREASES

- CHANGE ADAPTATION
- MANPOWER
- BASELINING PRICES
- LEGISLATIVE CHANGES
  - SYNOPSIS
  - SSJ APPROVALS
- UNIT PRICE INTEGRITY
- PSYCHOLOGICAL

Source: Department of Defense

MONTHLY AVERAGE PROCESSING DAYS
ALC - SMALL PURCHASES (UNDER $10,000)

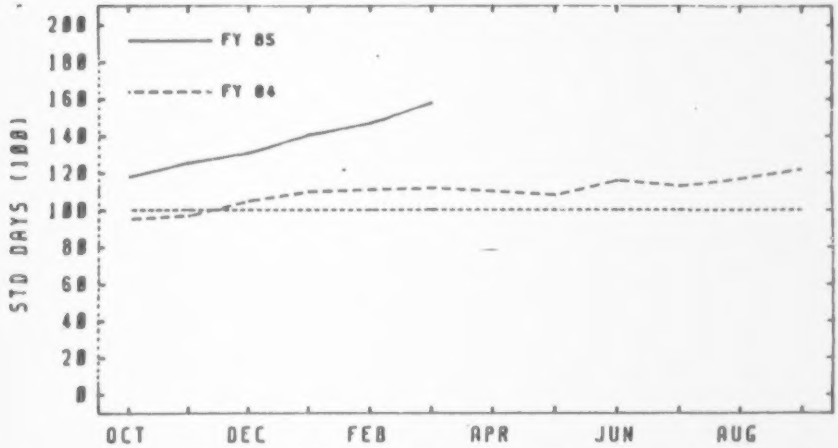


	OCT	NOV	DEC	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP
FY 85	82	94	98	102	107	118						
FY 84	60	59	60	65	68	67	67	66	73	75	78	84
FY 83	46	44	48	50	48	45	46	44	47	50	53	55

CHART A:ALCSMPUR.DYS

Source: Department of Defense

MONTHLY AVERAGE PROCESSING DAYS
ALC - NEGOTIATED CONTRACTS UNDER $100K



	OCT	NOV	DEC	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP
FY 85	118	126	131	141	147	158						
FY 84	95	97	105	110	111	112	110	108	116	113	117	122
FY 83	77	79	79	79	82	77	77	74	76	81	91	94

CHART A:ALCUS100.DYS

Senator **Quayle**. Thank you.

Our final witness on this panel is Bruce Hahn, manager for Government affairs, National Tooling and Machining Association.

STATEMENT OF BRUCE HAHN, MANAGER FOR GOVERNMENT AFFAIRS, NATIONAL TOOLING AND MACHINING ASSOCIATION, ACCOMPANIED BY PAUL SEIDMAN, PROCUREMENT COUNSEL, NATIONAL TOOLING AND MACHINING ASSOCIATION

Mr. **Hahn**. Thank you.

With me is Paul Seidman, procurement counsel for NTMA.

Our members are 14,000 small manufacturers who constitute the means of production in the United States. Their customer groups run the gamut from automotive to aerospace to appliance and defense.

We customarily submit sealed bids to our customers and they select the lowest bidder. This includes the defense prime contractors.

I would like to compliment this committee and Congress for the unanimous, and near unanimous in several cases, passage of the Competition in Contracting Act, the Small Business Competitive Enhancement Act, as well as amendments to last year's defense authorization.

The votes certainly reflect massive voter dissatisfaction with our current defense procurement system as well as the feeling of nearly 200 associations in the small business community that strongly feel more competition is necessary in defense procurement.

Among the $22 billion in annual procurement of spare parts are items like the $500 hammers, $1,000 nuts, $2,000 bolts, a piece of wire called antenna wire for $7,000 and an Allen wrench for $9,600. They come from many different sources, but one thing they share in common and that is their procurement was by sole source.

In fact, only about 10 percent of the $22 billion in spare parts procurement historically has been procured by the formally advertised sealed bid method.

SBA did a study of that 5 years ago and found that the average savings in these cases by switching from sole source to competitive bid was about 40 to 50 percent.

A GAO followup study confirmed that. What we are talking about, therefore, is the potential gross savings in the order of $8 to $9 billion per year if you can implement total competition in spare parts procurement, less something for overhead, of course.

It is our belief the implementation of last year's legislation is poor, that the problem is not necessarily in the legislation, although we feel more is needed, but in the implementation of the legislation.

Bascially nameless, faceless procurement policy-makers in the bowels of the Pentagon are making the rules that are making it very difficult to compete.

To give you an example, last year the Small Business Competition Enhancement Act, as well as the Defense Competition Act required the identification of actual manufacturers. The idea was to distinguish as to whether or not a part supplied to the Government was produced and actually made by the prime contractor or by a subcontractor.

In the implementation of that rule an actual manufacturer was defined as a company with design control over the part. It simply means the actual manufacturer is not necessarily the actual manufacturer which leads to the question why, therefore, identify the actual manufacturer?

The author of that particular language was obviously a fan of catch-22. We do not believe that there is a tremendous increase in competition out there, statistics provided by DOD notwithstanding.

For example, yesterday we called four chapters in our association in Indiana. Six of them in Michigan. Approximately 12,000 workers in Indiana, 19,000 in Michigan. We asked the chapter presidents, "Have you seen great increases in direct procurements for the Federal Government from our industry?"

Our members make up 70 percent of DOD spare parts as subcontractors. Let me give you some responses.

Evansville, no improvement.

Indianapolis, some improvement.

Muncie, no improvement.

Unable to reach Fort Wayne.

Grand Rapids, the president told us if they got one defense contract order among their members, they would consider it a surge.

Grand Rapids, have relatively little increase.

Unable to reach Kalamazoo.

No increase in Michigan City, IN.

No increase in Muskegon.

There is not a tremendous surge in the use of competition in spare-parts procurement. Another area of implementation of great concern right now is data rights. It is admittedly a complex area with varying ramifications for the various types of goods and services provided to the Government. It refers to such things as blueprints developed at private, public, or mixed expense.

Our members sell rights to their customers, both defense prime contractors and non-defense customers. Like the rights to a novel by a novelist, they are negotiable items. Our members often do not like to sell data rights that are legitimately theirs. They will. It is a question of price. Sometimes they do not.

The DAR Council for the first time in September drafted regulations, that will enable the Government to protect the legitimate interest of the taxpayer. Unfortunately, they caved in, taking away from procurement, from Defense Department buyers, an important tool that could be used to further competition in the future.

Our belief is that the system has been broken, despite sincere efforts of the small business community, Members of the Senate and House of Representatives to fix it.

There is legitimate doubt at this point as to whether the present system can be fixed. Therefore, we would suggest that the Congress of the United States should consider whether or not we might be better off establishing an independent procurement agency with new and sensible procurement policies and particularly new policymakers.

Thank you.

[The prepared statement of Mr. Hahn follows:]

PREPARED TESTIMONY OF BRUCE N. HAHN, NATIONAL TOOLING & MACHINING ASSOCIATION

Mr. Chairman and members of the Committee, my name is Bruce N. Hahn. I am Manager of Government Affairs and Public Relations for National Tooling and Machining Association. With me is Paul J. Seidman, Procurement Counsel for NTMA.

NTMA represents the tool, die and precision machining industry. This industry is composed of 14,000 plants almost all of which are small business concerns. These companies build special tools, dies, jigs, fixtures, molds, gauges, special machines (automation, robotics, and production lines) and precisioned machined parts or components. They use a wide variety of equipment and processes, including most machine tools from the simplest lathe to the most complex computer aided design and computer aided manufacturing systems. They commonly achieve tolerances to one ten-thousandth of an inch or less. These companies serve virtually every manufacturing industry in the country, from automotive to aerospace. Their customary means of doing commercial business is to provide sealed competitive bids from which the customer will generally select the lowest bid. Among our major customers are major DoD prime contractors, some of whom subcontract up to 80% of their spare parts to our members using competitive procurement procedures. The parts subcontracted are just as likely, if not more likely, to be the most critical and difficult parts. This is a reflection of the expertise in fabrication existing in our industry as well as the high level of skilled workers resulting from one of the largest industry wide skills training programs in America.

NTMA commends this Committee and the Congress for the enactment last session of the Competition in Contracting Act

(CICA), P.L. 98-369; provisions in the FY 1985 Defense Authorization Act (P.L. 98-525) aimed at curbing long ingrained abuses in spare parts procurement, and the Small Business Competition Enhancement Act of 1984, P.L. 98-577. These laws are designed to remove the bureaucratic barriers to the use of open competition.

Despite the recently enacted competition legislation and the documented potential for saving billions of dollars the opposition to the use of competition in procurement is still strong within DoD. It exists primarily where it always has -- among the nameless, faceless, mid-level bureaucrats in the bowels of the Pentagon. These individuals are still effective in frustrating the intent of Congress and the Administration. They are frustrating Congress by developing regulations which will be least effective in increasing competition. They are frustrating the Administration by providing biased information to key appointed decision makers. The technique employed is to block the flow of objective information to key decision makers and to substitute misleading and/or incomplete information which would lead any appointee not expert on this arcane subject matter to an erroneous conclusion.

In my testimony today, I will discuss the continued roadblocks presented to contractors attempting to compete for spare parts contracts. I will then address particular instances where the bureaucracy is thwarting last sessions' competitive procurement legislation. Such instances involve DoD rulemakers' regulatory implementation of Public Law 98-525 and 98-577 as those laws address (1) technical data reforms; (2) requirement that any prequalification requirement not exceed the minimum needs of the Government; and (3) requirement that the "actual manufacturer" of a spare part be identified. Also of interest is the Executive branches' implementation of the Competition in Contracting Act's provisions concerning (4) bid protest; and (5) Commerce Business Daily synopsis which have been respectively held to be illegal by a Federal Court and the General Accounting Office.

In addition, I would like to call this Committee's attention to proposed legislation that if enacted would materially frustrate competition. The first is the proposed amendments to the Freedom of Information Act (FOIA), set forth in S.150 which would make it unduly burdensome and costly for new sources to compete for spare parts procurement. The second is the Office of Federal Procurement Policy's proposed Simplified Competitive Acquisition Technique (SCAT). Under the guise of simplifying the procurement process SCAT would make it impossible for small businesses to obtain notification of requirements in time to bid and encourage contracting officers to award contracts through "competitive" negotiation where formal advertising should be used.

These points will be discussed in detail below.

I. Where's the Beef?

The well constructed legislation passed last year contained many elements which would increase the use of competition if properly implemented. However, our members continue to ask "where's the beef?" The lack of new opportunities has been confirmed with them as recently as our national meeting last month.

When we, along with nearly 200 other associations in the small business community, began the effort to increase competition in spare parts and other procurements, the services had a terrible track record. Only about 10% of the $22 billion in spare parts procurements were openly competed. This was particularly abhorrent inasmuch as actual case studies by SBA and GAO clearly demonstrated a savings of at least 40% by simply switching from sole source to competitive methods.

Recently, we have heard lots of statistics that suggest that the use of competitive procurement techniques have increased dramatically. The fact is that those statistics are meaningless. At our last convention, none of our members had noticed significant increases in competitive opportunities.

To see if things had changed, I called the Presidents of six of our Michigan chapters and four of our Indiana chapters yesterday. The four hundred companies in those two states would love the opportunity to compete for government business because they are severely impacted by foreign competition which is sapping the needs of their traditional customers in the automotive, appliance, and electronics industries. Those ten chapters have many, many shops which have had to lay off workers for lack of new business and they have noted no significant increase in competitive procurements.

NTMA member companies and other small businesses are ready, willing, and able to provide high quality spare parts to the Services at a fraction of the prices presently paid. However, they continue to be precluded from competing by bureaucratic impediments. Such impediments include the inability to obtain Government owned technical data in time to bid, the Services' refusal to provide technical data marked with unverified proprietary legends and whimsical qualification requirements which have absolutely no relation to the needs of the Government.

Even where DoD claims to "compete" spare parts contracts they rarely mean open competition with award to the lowest bidder. Less than 10% of the spare parts purchased by DoD are designated for purchase through open competition. What DoD means by "competition" is restricted competition with mindless prequalification requirements that are in many cases ultimately recommended and implemented by large original equipment manufacturers. This system has in effect limited "competition" for most spare parts to the OEM and subcontractors beholden to the OEM for their continued economic viability.

II. Examples of Improper Implementation of Recently Enacted Competition Legislation

A. Bureaucratic Subversion of P.L. 98-525 and P.L. 98-577 Technical Data Provisions

Although their work is not yet complete, bureaucratic subversion of Congressional intent is evidenced by interim implementation of the technical data provisions of the FY1985 Defense Authorization Act (P.L. 98-525) and Small Business Competition Enhancement Act of 1985, P.L. 98-577. NTMA's comments on the proposed rules concerning rights in data (DAR Case 84-187) and validation of rights in data (DAR Case 84-216 and FAR Case 85-47) are enclosed as **Exhibits 1 and 2.**

Early drafts circulated within the bureaucracy subverted Congressional intent by increasing rather than decreasing prime contractor rights in data and thus making competitive spare parts procurement more difficult. This would have been done by replacing the present rule under which the Government obtains "unlimited rights" if there is any Government money in the development of a part with a rule requiring 100% Government funding in order for the Government to have rights in data. It would even have discouraged obtaining data with unlimited rights where the Government had provided 100% funding!

These anticompetitive draft provisions were ultimately rejected in the proposed technical data rule published in the Federal Register for public comment on September 10, 1985. The proposed regulation met the Congressional mandate of defining legitimate "proprietary interest" by defining what data was "developed at private expense." The definition of "developed at private expense" restated existing case law by requiring "complete development ... without direct Government payment."

However at an October 1 meeting sponsored by the Defense Acquisition Regulatory Council, large aerospace contractors argued that the competition legislation passed last session was intended to give them more data rights rather than increase competition. Rather than define legitimate proprietary interests as mandated by the Congress DoD caved in and issued an interim rule which leaves this important concept undefined.

The really bad news for the taxpayer is in the interim technical data regulations promulgated by DoD which are substantially identical to those proposed for permanent inclusion in the Federal Acquisition Regulation. In enacting last years' procurement legislation, Congress intended to give contracting officers the tools necessary to eliminate noncompetitive procurements resulting from data mismarked as proprietary. As evidenced by testimony in numerous hearings, improperly marked data is a major barrier to the competitive purchase of spare parts. Unfortunately the interim rule promulgated by DoD allows the use of procedural artifices to delay the use of improperly marked data for competitive procurement for years.

The interim validation rules give contracting officers less authority to challenge claims to rights in data than that available to any member of the public under the Freedom of Information Act. Under the FOIA the Government is required to promptly release data absent adequate justification for any proprietary claims. Companies in the tooling and machining industry have recently used the FOIA to remove restrictive legends on thousands of spare parts.

Under the interim and proposed validation procedures a contracting officer desiring to challenge questionable data rights claims would be better off submitting an FOIA request for the data. This is obviously not what Congress intended when it enacted Public Laws 98-525 and 98-577.

DoD has extended the notice and comment period for the final rule until January 9, 1985. During this extended comment period and subsequent period for evaluating comments the procurement policy makers will no doubt continue their efforts to use last sessions' competition legislation as grounds for rules that would decrease the Government's rights in data and thereby decrease competition.

B. Improper Implementation of Limitations on Prequalification Requirements

Despite the enactment of Public Laws 98-525 and 98-577, prequalification continues to be a major barrier to the competitive purchase of spare parts by the military. A small businessman simply cannot afford to invest substantial sums to meet whimsical requirements to prequalify his firm or product for the mere privilege of bidding.

Public Laws 98-525 and 98-577 limit prequalification requirements to those least restrictive to meet the purposes necessitating the establishment of the qualification requirements. However under current procedures for qualifying sources to manufacture critical parts a contractor must have made a part before in order to be approved as a source. This requirement generally operates to limit "competition" to subcontractors which have made a part for a prime contractor.

Only the Services procure in this manner which is akin to limiting a contract for a painting of a particular mountain to only artists which have painted a picture of such mountain in the past. NTMA has a computerized system used by industry to match critical requirements with qualified sources. The system is based on what is needed to manufacture a particular item with vendor capabilities. Unfortunately, our offer to provide our system as a supplement or as a prototype of a model to identify qualified sources has to date not been accepted by the Services.

The imposition of unrealistic prequalification requirements appears to result from ignorance as well as intransigence on the part of contracting officials. One particularly disturbing consistent observation we learned from senior buyers at several procurement activities was that those activities are not only short of personnel, but that the compensation levels and job descriptions virtually preclude the hiring of individuals qualified to evaluate vendors of critical spare parts. Despite this, senior personnel in buying activities felt that it would be fruitless to try to convince the Office of Personnel Management to review job descriptions or to try to convince senior DoD or Service branch personnel to shift their interest from high tech whistles and bells to economically sound investment in appropriate numbers of qualified engineering personnel.

Frustrated by this experience we just obtained employment applications of 160 individuals responsible for engineering source approval at Kelly AFB, San Antonio, Texas. Although we had requested this information under the Freedom of Information Act many months ago its recent arrival precluded the thorough analysis it deserves in time for my testimony here today.

Nevertheless, one member experienced in the manufacture of critical spare parts reviewed the applications of the forty individuals responsible for propulsion systems and concluded that only one individual appeared fully qualified, and two others were marginally qualified. The rest of the applications, in his opinion, indicated little or no education or experience in the engineering disciplines required to produce precision machine parts. These disciplines include production process planning, quality engineering, and inspection techniques.

This is not a personal reflection on those individuals, some of whom have outstanding qualifications in other areas. Some may have had subsequent education or on the job experience which might have improved their initial qualifications. Nevertheless, it appears that 37 of 40 people making critical decisions on hot jet engine parts had no education or practical experience in the production disciplines required to build precision machine parts when they were hired.

Is it any wonder that someone in such a position would be highly reluctant to go anywhere but back to a large prime contractor for the purchase of parts or for approving alternative sources? There are thousands of qualified engineers the services could hire. Many such individuals are presently employed in the private sector. They could be enticed to work for the government, if proper levels of compensation were available.

C. DoD Has Improperly Implemented the Requirement that Prime Contractors Identify the "Actual Manufacturer" of a Part

In order to facilitate competition in future procurements, Public Laws 98-525 and 98-577 require that a prime contractor identify the "actual manufacturer" of a part if they do not manufacture it. This requirement is important because most prime contractors do virtually all the design and most of the assembly, but subcontract the manufacture of most parts to small businesses the Services are reluctant to contract with directly.

The regulation governing the acquisition of spare parts by DoD eliminates the requirement of identifying the actual manufacturer by defining "actual manufacturer" as a manufacturer "having design control responsibility for the part." The definition further states that "The actual manufacturer may produce the part in-house or by subcontracting." (Emphasis added) DFARS Supplement 6 §6-103.3.

Under this definition the OEM qualifies as the "actual manufacturer" of a part even if it does not manufacture it because it is invariably the design control activity. When we see interpretations like this, we wonder if the author is not related to the author of "Catch 22" and our suspicion that the regulations are developed by individuals with no interest in competition are once again confirmed.

In a June 19, 1984, GAO Report entitled "Analysis of Selected Sections of DOD's Revised Breakout Regulation" (GAO/NSIAD-84-138) GAO recommended that DoD "reassess its definition of 'actual manufacturer'." GAO's stated rationale was that defining actual manufacturer as the design control activity "may inhibit breakout because a contractor who controls the design, but does not actually produce the part, can be designated as the actual manufacturer." Unfortunately, GAO's recommendation has not been implemented.

D. Executive Branch Refusal to Implement CICA GAO Bid Protest Provisions

One of the most frustrating experiences for potential bidders is the absence of an effective and economical means of challenging agency procurement practices that are unduly restrictive of competition or otherwise improper. Because of the prohibitive cost of litigation, most small businesses utilize GAO bid protests to challenge noncompetitive DoD practices. These protesters are performing a public service because noncompetitive practices almost invariably result in unnecessary Federal expenditures.

Prior to the enactment of the CICA GAO Bid Protests were ineffective. Protests were not timely decided because despite a GAO rule requiring an agency response in 25 working days, contracting officials responded to protests whenever they pleased. Since a protest did not stay an award until it was decided an award was often made before a protest was decided. Thus, even if a protester prevailed at GAO, more often than not he was deprived of the fruits of his labor because an award had already been made. Despite the public benefit resulting from successful protests, there was no statutory basis for successful protesters to recover their attorneys fees.

In enacting the CICA Congress sought to remedy these deficiencies by statutorily requiring agencies to respond to protests within 25 working days, staying award until a protest is decided and giving GAO the authority to award attorneys fees to successful protesters. The enactment of these provisions should have provided a means for protestors to halt costly noncompetitive procurements.

However, the Justice Department on October 17, 1984 sanctioned continued Federal waste by issuing a memorandum directing agencies not to comply with the bid protest stay and attorneys fees provisions contained in the CICA on grounds that they are unconstitutional. This was shortly followed by a December 17 memorandum to agency heads from OMB Director David Stockman. The Stockman Memorandum directed agencies to ignore the law and follow the Justice Department position. Implementation was ordered by a U.S. District Court on March 27, 1985. Ameron, Inc. v. Army Corp of Engineers, DC NJ No. 85-10644A, decided May 28, 1985. As a result of the Court decision the Justice Department and OMB withdrew their directives ordering agencies not to comply with the CICA.

To the best of our knowledge, this is the first time that high ranking officials have directed Federal employees to violate Federal statutes. Without official encouragement from the Justice Department and OMB, DoD contracting officials have already wasted billions as a result of blatantly ignoring competitive bidding rules. Absent the Court order directing compliance with the law they would no doubt have risen to the opportunity offered by these curious actions from the supposed enforcer of the law and protector of public funds.

E. Implementing Regulations Water Down CICA Commerce Business Daily Synopsis Provisions

Another example of bureaucratic subversion of the intent of Congress involves the FAR provisions implementing the Commerce Business Daily improvements in the CICA and P.L. 98-72. The purpose of these provisions, for which the small business community fought long and hard, is to assure that small businesses receive notice of opportunities in time to bid. In order to achieve this objective it prohibits agencies from issuing a solicitation until 15 days after publication of a CBD synopsis.

Although Congress clearly intended that the CICA require contracting officials to determine that a synopsis was in fact published before issuing a solicitation, implementing regulations permit them to presume that a synopsis was published 10 days after transmission to the Department of Commerce. FAR §5.203(f). As a result of this rule millions in sole source orders that apparently never appeared in the CBD have been repeatedly awarded. When asked if the requirements were synopsized, contracting officers repeatedly state they do not know, but that the agency had met its legal obligations by forwarding a synopsis to the Commerce Department.

On September 24, 1985 the General Accounting Office held that that the Federal Acquisition Regulation's presumption of synopsis was contrary to recent statutory enactments and that the date on which notice is actually published controls in determining whether an agency has met its synopsis obligation. Aul Instruments, Inc., B-216543, 9/24/35. The Government has not yet indicated whether it will follow this GAO decision and this regulation has not been changed. Contracting officials continue to utilize the presumption of synopsis to frustrate competition.

III. The Congress Should Not Pass Proposed Legislation Which Inhibit Competition

A. Proposed FOIA Amendments Would Frustrate Access to Government-Owned Technical Data Needed to Compete for Spare Parts Contracts

On January 3, 1985, Senator Orrin Hatch introduced S.150, entitled the "Freedom of Information Reform Act." A similar bill passed the Senate last session.

If enacted, S.150 would be highly detrimental to small businesses that obtain Government-owned technical data from Service data repositories to bid on spare parts contracts. S.150 would eliminate the current FOIA fee ceiling of the direct cost of search and duplication. This limitation on FOIA fees was added by Congress in 1974 to curtail the prevalent bureaucratic practice of using high fees to frustrate requests for disclosure.

S. 150 would provide for the recoupment of all costs, including "services involved in examining records for possible withholding or deletions to carry out determinations of law or policy." In the case of commercially valuable information such as technical data, it would permit the Government to charge "a fair value fee or royalties or both, in addition to or in lieu of any processing fees otherwise chargeable." Thus in order to obtain technical data to bid, small businesses would likely have to pay a portion of the Government's research and development expenditure and this could cost thousands and eliminate competitive bidding for all practical purposes.

S.150 would also relax FOIA time limits at a time when agencies are taking months to respond to requests for procurement data. The time for bidding is generally 30 days.

S. 150 should be rejected because it would undo much of the good work in the area of procurement done by this Committee and the Congress last session. Given this Committee's role in the procurement area it might consider taking an offensive approach and report a bill which would guarantee prompt access to technical data needed by would be bidders independent of the FOIA. We would be glad to work with you on this. Such a provision should provide that such data is to be provided free, or at the minimum limit fees to the direct cost of search and duplication.

B. OFPP's Simplified Competitive Acquisition Technique

We are also concerned about the legislation that would establish a "Simplified Competitive Acquisition Technique" (SCAT) which was recently sent to the hill by the Office of Federal Procurement Policy. NTMA's August 19, 1985 comments to OFPP on SCAT appear as **Exhibit 3.**

Unlike large businesses which can afford onsite representation at procuring activities, small businesses for all practical purposes must learn of contracting opportunities through the CBD. SCAT would reduce the required period for CBD synopsis for covered procurements from the 15 day notice and 30 day response period mandated by last sessions' Competition in Contracting Act to a 5 day notice and 15 day response period.

The proposed reduction in CBD synopsis periods for SCAT procurements are unreasonable and will materially reduce competition. Despite the recent increase in the required synopsis time frames, NTMA member companies still have a problem learning of procurement opportunities and obtaining bid sets in time to submit a bid or proposal. This is especially true of spare parts contracts where it generally takes about six months to obtain technical data needed to bid from DoD data repositories. (OFPP would take a giant step towards increasing competition by requiring that technical data always be included with bid sets rather than spending time on this dubious legislative initiative.)

NTMA also objects to SCAT because it would decrease the use of formal advertising by making negotiation the path of least resistance. "Competitive" negotiation is no substitute for formal advertising because negotiation permits subjective evaluation criteria to steer contracts to favored sources. "Competitive" negotiation also permits contracting officials that are dissatisfied with the apparent successful offeror to reopen negotiations and solicit an additional round of best and final offers.

CONCLUSION

After an involvement of over three years in efforts to increase competition in government procurement, there is a legitimate question as to whether the current DOD procurement system can be fixed. Meetings during this period with procurement policy makers at DOD, with the service branches, and even with senior appointees, have not resulted in meaningful changes. The Department of Defense has resisted legislative changes despite actual votes which reflected the unanimous conclusion of both Houses of Congress that changes were necessary. Despite the clear intent of Congress, the rulemaking effort of procurement policymakers thus far is one which shows in some cases a deliberate effort to frustrate congressional intent and in other cases an appalling cowardice and disregard for the interests of the taxpayer.

For these reasons, we believe that it is perhaps time to ask whether the current system can be reformed. Perhaps what is needed is a brand new independent Defense procurement agency which could be set up right the first time. If it were staffed by new procurement policymakers from high tech but non defense areas we could perhaps come up with policies that would make sense, eliminate needless duplication in Service branches, and save the taxpayers billions of dollars each year. In the absence of a significant change in direction in the Department of Defense and the Service branches in the coming months we would suggest that the process begin.

This concludes my prepared statement. If you have any questions, I would be happy to answer them.

EXHIBIT 1

NATIONAL TOOLING &
MACHINING ASSOCIATION

9300 LIVINGSTON ROAD, FT. WASHINGTON, MD 20744
301/248-6200

October 1, 1985

Mr. Charles Lloyd
Executive Secretary
Defense Acquisition Regulatory Council
DASD(P-DARS)
c/o OUSDRE (M&RS)
Room 3D139
The Pentagon
Washington, D.C. 20301-3062

RE: DAR Case 84-187

Dear Mr. Lloyd:

The National Tooling & Machining Association appreciates this opportunity to submit these comments on the proposed revisions to DoD FAR Supplement provisions concerning technical data set forth in DAR case 84-187. Because of the abbreviated comment period these partial comments are submitted for purposes of the October 1, 1985 public meeting and will be supplemented shortly.

NTMA represents the tooling and machining industry. This industry is composed of 14,000 plants almost all of which are small business concerns. These companies build special tools, dies, jigs, fixtures, molds, gauges, special machines (automation, robotics, and production lines) and precision machine parts or components. They use a wide variety of equipment and processes, including most machine tools from the simplest lathe to complex electrical-chemical milling, and electron-beam welding. They commonly achieve tolerances to one ten-thousandth of an inch and regularly use computers as an aid in design, machining, and control of operations.

The tooling and machining industry is the cornerstone of modern mass production. The 14,000 companies in the industry serve virtually every other industry in the nation, from automotive to aerospace. Without the services of these thousands of highly competitive small companies mass production would not exist.

NTMA member companies are ready, willing and able to provide the Services with high quality spare parts at a fraction of prices presently paid and with materially shorter lead times.

However they have been repeatedly been precluded from bidding because the Government has incomplete data or because of prime contractor claims to rights in data.

Less than 10% of the approximately $22 billion spent by the Services on spare parts is awarded through open competition. Considering that costs savings of one-half have repeatedly been documented when spare parts contracts are openly competed the need for Government ownership of data rights is obvious.

Many of these problems were addressed in Public Laws 98-525 and 98-577 and this proposed implementing regulation. We urge that DoD not permit this rulemaking effort to be used to gut the competitive procurement legislation passed by the Congress at the urging of the small business community.

In response to the announcement of a public meeting published in the Federal Register of September 20, 1985 these preliminary comments will address the substance of the proposed regulation as well as advisability of an alternate interim rule. These comments are written from the perspective of small businesses in the tooling and machining industry that want to bid on DoD spare parts procurements. While they are undoubtedly appropriate for the procurement of many other goods and services the limited time allowed has precluded an across the board evaluation.

I. Preliminary Comments on the Proposed Regulation

NTMA is generally pleased with the DAR Council's draft implementation of the technical data provisions contained in P.L. 525 and 98-577. As you know these provisions were enacted to increase competition in Federal contracting and prevent spare parts procurement abuses. Our comments concerning particular portions of the draft regulation are set forth below following a background discussion of what constitutes a fair technical data policy and the public interest in acquiring data for purposes of competive procurement. We intend to supplement these comments at a later date after we have had the opportunity to more completely review the proposed regulation.

A. Background--Fairness and the Public Interest

Before making specific comments and recommendations it is appropriate to make some remarks on fairness and the public interest in obtaining data for competitive procurement.

In private industry a vendor with proprietary rights may wish to sell a product produced with such rights to another company without any data rights. This will suit the buyer in many cases. On the other hand the buyer often desires to purchase or obtain a license in the sellers proprietary rights and build the product itself. If the buyer and seller are unable to reach an agreement the buyer can seek an alternative vendor and the seller other customers.

As long as both buyer and seller have the right to determine what they will or will not accept the relationship is a fair. Thus the question of what data the Services do or do not require is not a question of fairness. Just as in the in the case of private companies it is a matter of determining what is in the best interest of the buyer, which in this case is the taxpayer and the seller.

The proposed regulations are more favorable to sellers than private sector practices because they never force a contractor to part with rights to data they do not want to provide in order to obtain a contract. More specifically §227.472 (b) expressly provides that offerors shall not be required to provide data developed at private expense as a condition of obtaining a contract. Where data rights to be provided the Government are an evaluation factor the proposed regulations leave a contractor free in all instances to either submit a proposal in which it retains rights to all items developed at private expense, include fair compensation for such rights in data in their price to the Government, or not bid.

We believe that a contractor's willingness to part with data developed at private expense for components to major systems should be a key evaluation factor in every instance for items that will be reprocured at a later data. The acquisition of data developed at private expense will result in considerable savings through the competitive procurement of replenishment parts. It will also give DoD and the Congress a better idea of the true cost of weapons systems up front. Today the initial acquisition cost is no more than a down payment and the true cost is learned later when the Services learn the cost of purchasing spares noncompetitively.

B. Definition of "Developed at Private Expense"

§227.471 of the proposal defines "developed at private expense" in order to meet the P.L. 98-525 requirement of defining legitimate proprietary interest. The requirement that an item, component or process be brought to the point of practical application in order for it to be considered to be "developed at private expense" is vital and should not be weakened.

The requirement of "completed development ... without direct Government payment" in order for a contractor to claim proprietary rights is consistent with the requirement that an item be brought to the point of practical application in order to be patentable. Such a requirement is necessary to protect the taxpayer since few ideas ever reach the patent stage and of those that do only a few achieve market acceptance which is the only true measure of their value.

Furthermore the requirement of completed development at private expense in order for a contractor to retain rights in data merely restates interpretations of existing regulations under which the Government gets unlimited rights when development is accomplished with a mixture of contractor and Government funds. Surely the Congress did not intend to dilute the Government's rights when it passed this remedial legislation.

If anything the proposed regulation may not go far enough because it looks to each separate element of an an item component or process separately to determine if it was "developed at private expense." The DAR Council should consider eliminating this loophole to avoid the "swiss cheese" drawings (drawings where portions are omitted as proprietary) that have previously perpetuated costly, noncompetitive spare parts procurements.

C. "Limited Rights" Definition

We endorse the clarification of the definition of "limited rights" contained in §227.471 which permits the Services to release data to contractors hired to evaluate any claims to rights in data. Such release is of course subject to the prohibition against further disclosure. From our visits with Competition Advocates at several Air Logistics Centers it is clear that they often lacked the resources to challenge possible spurious claims to rights in data that have caused noncompetitive buys. This provision would expressly allow them to accomplish this function by contracting it out to persons in the private sector with the necessary expertise.

D. Policy Statement

The policy statement in §227.472(a) provides that DoD "shall acquire only such technical data and computer software and rights therein as are essential to meet the Government's missions, including the interest of the United States in increasing competition and lowering costs by developing and locating alternative sources of supply and manufacture." This statement is too weak. Although competition almost always is in the Government's best interest it is rarely "essential to meet the Government's missions."

We recommend that the policy statement in §227.472(a) be beefed up to reflect the remedial intent of Public Laws 98-525 and 98-577. This could be done by revising §227.472(a) to state that "The Department of Defense shall acquire such technical data and rights therein as is in the Government's best interest. In determining the Government's best interest the interest of the United States in broadening the industrial base and lowering costs by developing and locating alternative sources of supply and manufacture should be balanced against the interest of the United States in fostering innovation."

E. Direct Licensing

§227.473-2(c) provides for direct licensing to new sources to enhance competition. For purposes of direct licensing the Government should have the right to select the licensee through competitive procedures. This is necessary to avoid situations where a licensee is a subcontractor forced to rely on the OEM licensor for its continued viability. Such situations do not result in true competition.

F. Expiration of Limited and Restricted Rights

§227.473-2(e) implements 10 U.S.C. §2320(c) by allowing DoD to negotiate a time limit on limited rights in technical data with a negotiation objective not to exceed seven years. This is a step in the right direction.

As previously discussed there is nothing wrong with the Services fairly compensating a contractor for data on items developed at private expense and thereby achieve savings through competitive procurement. In many cases such purchase should be negotiated from the outset as opposed to negotiating a time limit on contractor rights in data.

G. Unmarked or Improperly Marked Technical Data

§227.473-3(c) allows the contracting officer to invoke the data validation provisions of Public Laws 98-525 and 98-577. This provision adopts existing case law by requiring a contractor to prove its claims to rights in data by clear and convincing evidence.

We disagree with the contention that new regulations regarding validation of proprietary rights should recognize that Congress has discarded the requirement that contractors be able to support any claims to rights in data by clear and convincing evidence. This contention is remarkable in light of the fact that in enacting Public Laws 98-525 and 98-577 Congress was attempting to remedy the problem of costly, noncompetitive procurements caused by spurious claims to rights in data.

The clear and convincing evidence test should be retained. In light of past data abuses and their cost to the public we also recommend that the regulation provide for referral to the Department of Justice where mismarking of data appears to be intentional.

II. Advisability of an Interim Rule

The Department of Defense procurement mechanism has been rocked by scandal after scandal. The extremely low public credibility in procurement policies has no doubt been a factor in the erosion of support needed to fund a strong national defense.

It is to the credit of the Defense Acquisition Regulatory Council that these proposed regulations show an inclination to protect the taxpayers interest. While it would certainly be desirable to have more time to review the regulation this is clearly outweighed by the need to restore public credibility to the procurement rulemaking process.

NTMA therefore strongly recommends that the regulations be implemented by the statutory deadline. Refinements can be made at a later date in light of comments received from large and small businesses.

III. Other Matters

Because the small business community rarely has the opportunity to appear before the Defense Acquisition Regulatory Council we would like to briefly suggest some additional initiatives to enhance competition.

A. Modify DFARS Supplement No. 6 to Provide for Generic Qualification of Spare Parts Manufacturers

Under current procedures for qualifying sources to manufacture critical parts a contractor generally must have made a part before in order to be approved as a source. This requirement often limits "competition" to subcontractors which have made a part for a prime contractor.

Only the Services procure in this manner which is akin to limiting a contract for a painting of a particular mountain to only artists which have painted a picture of such mountain in the past. NTMA has a computerized system used by industry to match requirements with qualified sources. The system is based on matching what is needed to manufacture a particular item with vendor capabilities. Unfortunately our offer to use such system to identify qualified sources has to date been ignored by the Services.

B. Eliminate the Presumption of CBD Synopsis for DoD Procurements

In enacting Public Laws 98-72 and 98-369, Congress required that a solicitation not be issued until 15 days after synopsis in the Commerce Business Daily and that a solicitation remain open for at least 30 days after synopsis. This legislation was necessary in order to assure that small businesses obtain bid sets in time to bid. Congress undoubtedly meant actual synopsis as opposed to presumed synopsis.

However, FAR §5.203 permits a contracting officer to presume a requirement is synopsized ten days after it is transmitted to the Department of Commerce. Aside from being contrary to law, this provision has resulted in requirements not being synopsized or synopsized too late.

The DAR Council should urge the FAR Council to repeal this provision while promulgating a DoD rule that complies with Public Laws 98-72 and 98-369.

C. Improve Information Provided in Commerce Business Daily Synopsis

The Services repeatedly complain that they are forced to send out too many bid sets and therefore need to charge for bid sets. At the same time our members tell us that because of inadequate CBD synopsis they are forced to request bid sets for items they ultimately determine they are not interested in. The obvious best solution for all concerned is to improve CBD synopsis to enable firms to be more selective in the bid sets they request. We would be happy to work with you on this.

D. Permit Bid Sets to Be Requested by Telephone

The Services often do not get bid sets to would be bidders in time to bid. Part of this delay is caused by contracting officers requiring a written request for a solicitation. DoD regulations should be modified to allow requests to be made by telephone.

E. Require Technical Data to Be Included in all Solicitations

Delays and problems in responding to solicitation occur because Government-owned technical data is not included in bid sets for spare parts contracts. This frustrates competition because it often takes six months to get technical data from DoD data repositories. The obvious solution is to require by regulation that bid sets contain Government-owned technical data.

CONCLUSION

NTMA very much appreciates the opportunity to meet with and present this statement to the Defense Acquisition Regulatory Council. If you have any questions, or if we can be of further assistance, please let us know.

Sincerely,

Bruce N. Hahn
Manager
Government Affairs

EXHIBIT 2

NATIONAL TOOLING &
MACHINING ASSOCIATION

9300 LIVINGSTON ROAD, FT. WASHINGTON, MD 20744 301/248-6200

October 9, 1985

HAND DELIVERED
General Services Administration
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HAND DELIVERED
Mr. Charles Lloyd
Executive Secretary
Defense Acquisition Regulatory Council
DASD(P-DARS)
c/o OUSDRE (M&RS)
Room 3D139
The Pentagon
Washington, D.C. 20301-3062

RE: FAR Case 85-47
DAR Case 84-216

Dear Civilian Agency and DoD Rulemakers:

The National Tooling & Machining Association appreciates this opportunity to submit these comments on the proposed regulations implementing the technical data validation provisions set forth in Public Laws 98-525 and 98-577.

NTMA represents the tooling and machining industry. This industry is composed of 14,000 plants almost all of which are small business concerns. These companies build special tools, dies, jigs, fixtures, molds, gauges, special machines (automation, robotics, and production lines) and precision machine parts or components. They use a wide variety of equipment and processes, including most machine tools from the simplest lathe to complex electrical-chemical milling, and electron-beam welding. They commonly achieve tolerances to one ten-thousandth of an inch and regularly use computers as an aid in design, machining, and control of operations.

The tooling and machining industry is the cornerstone of modern mass production. The 14,000 companies in the industry serve virtually every other industry in the nation, from automotive to aerospace and computers to consumer goods. Without the services of these thousands of highly competitive small companies mass production would not exist.

NTMA member companies are ready, willing and able to provide the Services with high quality spare parts at a fraction of prices presently paid and with materially shorter lead times. However they have been repeatedly been precluded from bidding because of questionable claims to rights in data.

Less than 10% of the approximately $22 billion spent by the Services on spare parts have historically been awarded through open competition. Considering that costs savings of one-half have repeatedly been documented when spare parts contracts are openly competed it is essential that contracting officials have the tools necessary to challenge questionable claims to rights in data that perpetuate noncompetitive procurements.

In enacting Public Laws 98-525 and 98-577 Congress gave contracting officials new tools to combat noncompetitive procurements resulting from improper claims to rights in data. NTMA is in general agreement with the proposed implementation of the legislative provisions concerning validation of claims to rights in data. However, we believe that certain changes are necessary in order to best protect the taxpayer. More specifically in order to facilitate prompt removal of improper claims to rights in data we recommend that:

1. the prechallenge review procedure be made optional with the contracting officer; and

2. the provisions limiting the Government's right to use data after a contracting officer decision removing a restrictive legend be eliminated.

NTMA also urges that DoD and civilian agency rulemakers ignore the attempts to use these rulemaking proceedings to weaken contractor obligations to justify proprietary claims which predated Public Laws 98-525 and 98-577. In addition, we urge compliance with the Regulatory Flexibility Act in promulgating this rule which because of the noncompetitive aspects discussed herein has a significant economic impact on a substantial number of small business concerns. These points will be addressed in detail below.

I. The Prechallenge Review Procedure Should be Made Optional with the Contracting Officer

§27.409-1(c) provides that a contracting officer may send a a written challenge notice to a contractor "If after completion of the prechallenge review the contracting officer determines that a challenge to the restrictive marking is warranted... ." This would unnecessarily delay the removal of improper claims of rights in data since it appears to require the contracting officer to go through the pre-challenge review procedures even where he already has probable cause to challenge a contractor's proprietary claim. We believe this provision which is not a part of the statutes being implemented will unnecessarily delay the removal of improper restrictive legends and should be eliminated.

II. Limitations on the Government's Right to Use Data After a Contracting Decision Removing Restrictive Legends Should Be Eliminated

The proposed regulation provides that the Government will not use data even after a contracting officer decision removing restrictive legends if either a contractor within 90 days (1) appeals to the Board of Contract Appeals or (2) indicates it will appeal to the Claims Court within one year. After a suit is filed it provides that the data will not be used for competitive procurement until a final decision is issued. These provisions, which do not appear in either Public Law 98-525 or 98-577, would allow a contractor to delay having to face competition indefinitely and should be eliminated. Although the proposed regulations provide the data can be used in the interim upon a finding of "urgent or compelling circumstances" by the head of the agency in practice this is of little practical value to a contracting officer.

Under the proposed regulations it would be to a contractor's advantage in every instance to indicate it would it would file suit in the Claims Court within one year. Even if suit is never filed it delays release of data for one year without any penalty.

If suit is filed it can easily take years for a decision on the merits. Technical data litigation has in the past been characterized by repeated requests for time extensions by contractors. It also should be noted that a Board of Contract Appeals decision is not final until any appeal to the U.S. Court of Appeals for the Federal Circuit is decided.

These provisions give the contracting officer less power to challenge claims to rights in data than that available to any member of the public under the Freedom of Information Act.[1] Under the FOIA the Government is required to promptly release data absent adequate justification for any proprietary claims. Companies in the tooling and machining industry have recently used the FOIA to remove restrictive legends on thousands of spare parts.

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[1] We note that the Justice Department has repeatedly refused to defend the DoD position that technical data is not a record within the meaning of 32 C.F.R. §286.13(c)(2)(iii) and such position is no longer followed by the Navy and the Air Force.

If the validation provisions were promulgated in their present form a contracting officer desiring to challenge questionable data rights claims would be better off submitting an FOIA request for the data. This is obviously not what Congress intended when it enacted Public Laws 98-525 and 98-577.

It also should be noted that these provisions are not necessary to provide a contractor with an adequate remedy at law. If a contracting officer decision removing a restrictive legend is overturned a contractor is entitled to recover damages for any pecuniary loss.

III. These Rulemaking Proceedings Should Not Be Used to Weaken Pre-Existing Contractor Obligations to Justify Proprietary Claims

Public Laws 98-525 and 98-577 address the problem of noncompetitive procurements resulting from spurious contractor claims to rights in data by providing contracting officials with a statutory procedure to challenge such rights. Despite the remedial nature of this legislation some contractor representatives are attempting to use this rulemaking effort to weaken the Government's position under the rules which pre-dated Public Laws 98-525 and 98-577. We urge that DoD and Civilian agency rulemakers keep the taxpayers interest in mind and not permit this rulemaking effort to be used to gut this long needed competitive procurement legislation. Two areas of particular concern which will be discussed below are the attempt to eliminate the longstanding requirement that contractors justify proprietary claims by clear and convincing evidence and the suggestion that a time limit be placed on the Government right to challenge claims to rights in data.

A. The Requirement that Claims to Rights in Data Be Justified by Clear and Convincing Evidence Should Be Retained

Standard clauses have long required that contractors substantiate "the propriety of limited rights markings by clear and convincing evidence."[2] We disagree with the contention that new regulations regarding validation of proprietary rights should recognize that Congress has discarded the requirement that contractors be able to support any claims to rights in data by clear and convincing evidence. This contention is remarkable in light of the fact that in enacting Public Laws 98-525 and 98-577 Congress was attempting to remedy the problem of costly, noncompetitive procurements caused by spurious claims to rights in data.

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[2] See paragraph (d)(2) of the May 1981 DoD Rights in Data and Computer Software which appears at DFARS §5.227-7013.

The clear and convincing evidence test should be retained. As recently stated by the U.S. District Court for the District of Columbia in upholding the Navy's removal of contractor limited rights legends:[3]

> ...the contractor has the burden of maintaining records to support the use of the legends on data submitted under contract. If a contractor has developed data which it maintains is a trade secret, it is in the contractor's best interest to maintain records to show that the contractor fully paid for the development of that data in order to justify the use of the restrictive legends.

In light of past data abuses and their cost to the public we also recommend that the regulation provide for referral to the Department of Justice where mismarking of data appears to be intentional.

B. No Time Limit Should Be Placed on Contractor Justification Requirements

At the October 1, 1985 public meeting on DAR case 84-187 preliminary comments on the validation rule were sought by the DAR Council. One member of the audience suggested that a time limit be placed on the requirement that contractors justify claims to rights in data.

We believe it is in the taxpayers best interest to retain the present rule under which contractors are required to substantiate any claims to rights in data for as long as they assert them. It makes little sense to for the first time time place a time limit on substantiation requirements in implementing statutes aimed at combatting mismarked data.

A time limit on the contracting officer's authority to obtain susbtantiation would insulate contractors from challenges on older contracts where the limited rights stamp appears to have been freely used irrespective of contract provisions entitling the Government to rights in data. Until recent disclosure of spare parts horror stories such legends were routinely accepted by the Government without review or challenge.

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[3] Williams International v. Lehman, Civil Action No. 84-1122, slip op. at 20 (D.D.C. Nov. 6, 1984)2

IV. Regulatory Flexibility Act

For the reasons previously discussed, the proposed rule in its present form will unnecessarily delay the use of mismarked data for competitive procurement. Contrary to the Regulatory Flexibility Act statement appearing in the supplementary information section of the regulation, these noncompetitive aspects of the rule will have a significant economic impact on a substantial number of small business concerns. Therefore strict compliance with the requirements of the Regulatory Flexibility Act is required.

V. Other Matters

NTMA would like to take this opportunity to briefly suggest some additional initiatives to enhance competition for spare parts procurement. These suggested initiatives are set forth below.

A. Modify DFARS Supplement No. 6 to Provide for Generic Qualification of Spare Parts Manufacturers

Under current procedures for qualifying sources to manufacture critical parts a contractor generally must have made a part before in order to be approved as a source. This requirement often limits "competition" to subcontractors which have made a part for a prime contractor.

Only the Services procure in this manner which is akin to limiting a contract for a painting of a particular mountain to only artists which have painted a picture of such mountain in the past. NTMA has a computerized system used by industry to match requirements with qualified sources. The system is based on matching what is needed to manufacture a particular item with vendor capabilities. Unfortunately our offer to use such system to identify qualified sources has to date not been accepted by the Services.

B. Eliminate the Presumption of CBD Synopsis for DoD Procurements

In enacting Public Laws 98-72 and 98-369, Congress required that a solicitation not be issued until 15 days after synopsis in the Commerce Business Daily and that a solicitation remain open for at least 30 days after synopsis. This legislation was necessary in order to assure that small businesses obtain bid sets in time to bid. Congress undoubtedly meant actual synopsis as opposed to presumed synopsis.

However, FAR §5.203 permits a contracting officer to presume a requirement is synopsized ten days after it is transmitted to the Department of Commerce. Aside from being contrary to law, this provision has resulted in requirements not being synopsized or synopsized too late.

The provision should be repealed.

C. Improve Information Provided in Commerce Business Daily Synopsis

The Services repeatedly complain that they are forced to send out too many bid sets and therefore need to charge for bid sets. At the same time our members tell us that because of inadequate CBD synopsis they are forced to request bid sets for items they ultimately determine they are not interested in. The obvious best solution for all concerned is to improve CBD synopsis to enable firms to be more selective in the bid sets they request. We would be happy to work with you on this.

D. Permit Bid Sets to Be Requested by Telephone

The Services often do not get bid sets to would be bidders in time to bid. Part of this delay is caused by contracting officers requiring a written request for a solicitation. DoD regulations should be modified to allow requests to be made by telephone.

E. Require Technical Data to Be Included in all Solicitations

Delays and problems in responding to solicitation occur because Government-owned technical data is not included in bid sets for spare parts contracts. This frustrates competition because it often takes six months to get technical data from DoD data repositories. The obvious solution is to require by regulation that bid sets contain Government-owned technical data.

CONCLUSION

NTMA very much appreciates the opportunity to present this statement to the Civilian Agency and Defense Acquisition Regulatory Councils. If you have any questions, or if we can be of further assistance, please let us know.

Sincerely,

Bruce N. Hahn

Bruce N. Hahn
Manager
Government Affairs

EXHIBIT 3

NATIONAL TOOLING &
MACHINING ASSOCIATION

9300 LIVINGSTON ROAD, FT. WASHINGTON, MD 20744 301/248-6200

August 19, 1985

Mr. William J. Maraist
Associate Administrator
Office of Federal Procurement Policy
New Executive Office Building
Room 9025
726 Jackson Place, N.W.
Washington, D.C. 20503

Dear Bud:

Thank you for meeting with us to discuss the proposed Simplified Competitive Acquisition Technique Act of 1985. As we discussed, although we concur with the need for more simplified procurement procedures, we believe that unless SCAT is significantly modified it will reduce procurement efficiency. Our comments on the various aspects of SCAT, as well as some additional suggestions for procurement reform are set forth below.

Recommendations re SCAT

1. The Proposed Reduction in the Period for CBD Synopsis is Unworkable

SCAT would reduce the period for CBD synopsis from the current 15-day notice and 30-day response period to a 5-day notice and 15-day response period. This repeals the recently enacted CBD improvements for SCAT procurements.

The proposed reduction in CBD synopsis periods for SCAT procurements are unreasonable and will materially reduce competition. Despite the recent increase in the required synopsis time frames, NTMA member companies still have a problem learning of procurement opportunities and obtaining bid sets in time to submit a bid or proposal. The advantage of the timely CBD synopsis is that sole source procurements (and even negotiated procurements) could be converted into fully competitive procurements. The two advantages when that happens are lower costs and faster deliveries. There is ample documentation that total time (advertising/negotiation, production and delivery) is significantly faster and that costs are significantly lower.

Another problem that you should consider in reducing the time for bidding is that technical data is often not contained in bid sets and therefore must be obtained from DoD data repositories. This is especially true of spare parts contracts. It generally takes about six months to obtain technical data needed to bid on spare parts contracts from DoD data repositories. Contracts where technical data is not included in a bid set should not be subject to an expedited procedure such as SCAT. Better yet OFPP would take a giant step towards increasing competition by requiring that technical data always be included with bid sets. We would very much support language to that effect in any proposed legislation.

2. SCAT Would Encourage Negotiation Where Formal Advertising Should be Used.

SCAT would likely decrease the use of formal advertising (the "sealed bid method") by making negotiation the path of least resistance. "Competitive" negotiation is not substitute for formal advertising because negotiation permits subjective evaluation criteria and multiple round of best and final offers to be used to steer contracts to favored sources. SCAT should state that it is not a substitute for formal advertising. In addition, any streamlined procedures included in SCAT should be extended to formal advertising to encourage its use.

3. Elimination of Pre-award Audit Requirements

The elimination of pre-award audit requirements is positive. However, it is not substitute for using formal advertising with award to the lowest bidder.

4. Making the Contracting Officer the Final Selecting Authority Should Not Deprive Small Businesses of their Right to a SBA COC or Size Determination Procedures.

The proposed legislation would make the contracting officer the final selection authority and thereby apparently deprive small businesses of their statutory right to have the SBA make the final determination of their capability to perform under its COC program, as well as access to SBA size determination procedures. SBA certificate of competency reviews are necessary because of the tendency of contracting officials to underestimate the capability of small business concerns. COC reviews have resulted in substantial savings because of resulting awards to the low bidder. Access to small business size protest and appeal procedures is also necessary to maintain the integrity of the small business set-aside process.

Although you indicated SCAT would not impact the right of a small business to a COC review, or access to size protest and appeal procedures, clarifying language is necessary to avoid this result.

5. Limiting Solicitation to 20 Pages is of No Value if Achieved by Incorporating Clauses by Reference

Limiting solicitations to 20 pages does not accomplish anything if it is done by incorporating contract clauses by reference. If anything it creates a new problem because contractors will be forced to obtain copies of contract clauses within an abbreviated bidding period.

What is needed is a 20 page, plain English solicitation with no incorporation by reference. This could be accomplished by raising the dollar threshold for various socio-economic requirements to a level where administration is cost effective.

6. Requiring Protests to be Filed with the Contracting Officer First May Take More Time. If Included, This Requirement Should Not Impact Subsequent Access to Other Remedies.

Requiring protests to be filed with the contracting officer first might have the unintended result of lengthening the procurement cycle. Protests are often not filed with the contracting officer first because he has already informally indicated he will not alter his position. When a protest that would otherwise have originally been filed at GAO, in Court or at the General Services Board of Contract Appeals (GSBCA) is denied by the contracting officer, the process will be forced to start again where it could have begun in the first instance. If a protest is filed at GAO, Court, or the GSBCA first, a contracting officer can always change his position if he believes the protest to be meritorious.

The requirement that protests be filed with the contracting officer first could be used to deprive bidders of their right to challenge the contracting officer in the Claims Court or their right to obtain a stay of performance under GAO rules implementing the Competition in Contracting Act. Modifications are necessary to prevent this unintended result.

More specifically, a contracting officer could deprive a contractor of his right to bring suit in the Claims Court by denying a protest and immediately making an award. The Claims Court only has jurisdiction before an award is made. The SCAT proposal should be modified to provide a period for filing in the Claims Court if a protest is denied by the Contracting officer.

Under the Competition in Contracting Act, P.L. 98-369 a protestor is only entitled to have performance stayed if a protest is submitted to GAO within ten days of award. A contracting officer could under SCAT frustrate any meaningful view of his actions by not informing a contractor of the fact that his protest has been denied until ten days after award. This could be remedied if SCAT provided that an award could not be made until ten days after receipt of notification that a protest to the contracting officer has been denied.

Other Recommendations

1. Eliminate the FAR Presumption of CBD Synopsis

In enacting Public Laws 98-72 and 98-369, Congress required that a solicitation not be issued until 15 days after CBD synopsis and that a solicitation remain open for at least 30 days after synopsis. This legislation was necessary in order to assure that small businesses obtain bid sets in time to bid. In requiring synopsis, Congress undoubtedly meant actual synopsis as opposed to presumed synopsis.

However, FAR 5.203 permits the contracting officer to presume a requirement is synopsized ten days after it is transmitted to the Department of Commerce. This FAR provision should be repealed. Aside from being contrary to law, this provision has resulted in requirements not being synopsized or synopsized too late.

2. Improve Information Provided in CBD Synopsis

DoD personnel repeatedly complain that they are forced to send out too many bid sets and therefore need to charge for bid sets. At the same time our members tell us they are forced to request bid sets for items they ultimately determine they are not interested in. The obvious best solution for all concerned is to improve CBD synopsis to enable firms to be more selective in the bid sets they request. We would be happy to work with you on this.

3. Permit All Bid Sets to be Requested by Telephone

SCAT would permit telephonic requests of bid sets for SCAT procurements only. This is a clear improvement over existing procedures and should be extended to all procurements.

4. Require Technical Data to be Included in all Solicitations

As previously noted, delays and problems in responding to solicitations occur because Government-owned technical data is not included in bid sets. This frustrates competition because it normally takes six months to get technical data needed for bidding from DoD date repositories. The obvious solution is to require that bid sets include Government-owned technical data.

5. Reduce Bid Set Posting Requirements to $2,500

FAR 5.101 increased the dollar threshold for posting bid sets for contracts to be let to $10,000 from the $2,500 previously in the DAR and FPR. Such provision where followed, makes it virtually impossible to learn of opportunities below the $10,000 threshold for synopsis in the Commerce Business Daily.

The posting threshold should therefore be reduced to the prior level of $2,500.

Conclusion

Although we applaud OFPP's efforts to simplify the procurement process, we believe that SCAT requires substantial modification if it is to achieve such a result without reducing competition.

As you know we have been deeply involved with procurement issues for several years, and served as the focal point for a coalition of nearly 200 associations from the small business community which was, in a large degree, responsible for much of the procurement reform legislation enacted last year. We intend to maintain our visible role. It would seem to make sense for us to work together in developing legislation we can all support rather than to find ourselves on the opposite side of a highly visible public issue. In summary, we are suggesting that we begin a process of dialogue and negotiation prior to the introduction of this proposal.

NTMA appreciates the opportunity to have met with you and present these comments. If you have any questions, or if we can be of further assistance, please let me know.

Cordially,

E.L. Hardman

William E. Hardman
President and Chief Operating
Officer

WEH/mw

cc: Honorable Lowell Weicker, Chairman, Senate Small Business Committee
Honorable Parren Mitchell, Chairman, House Small Business Committee
Honorable William Roth, Chairman, Senate Governmental Affairs Committee
Honorable Jack Brooks, Chairman, House Government Operations Committee
Honorable Barry Goldwater, Chairman, Senate Armed Services Committee
Honorable Les Aspin, Chairman, House Armed Services Committee

Senator QUAYLE. Thank you very much, Mr. Hahn. I think that an independent agency is certainly a possibility.

Having listened to the testimony here today and the other past days, I just wonder if such an agency would not create more bureaucratic regulation, less small business involvement, less competition.

It is an idea, but one that I have a great deal of skepticism about personally. I think we have to work to try to make the current system far more efficient than it is.

This is the fourth day of hearings that we have had. We will read your testimony very closely. I would imagine we will probably go along with repeal and modification of the legislation that Mr. Clark talked about on Public Law 98-525.

There is nothing terribly wrong with the legislation itself, but the way it is implemented, in fact, gives us a lot of problems. I am not sure that we have been terribly specific on what regulations or what things in the Department of Defense you say to cut out or do away with.

What we have here is a rather interesting cycle. The Congress in response to perceptions of problems is passing legislation which is to an extent micromanagement, but some of it is really trying to beef up personnel and help us get a better industrial base.

I think the goals of the legislation are supported by all. There may be a dispute on how the legislation is actually written, but the goals are supported by all.

Once it gets over to the Department of Defense, then the interpretation therein sort of goes overboard. We get a lot of problems and then you folks are the ones that have to do business with the result.

So, we call and ask: "What are we going to do about it?" Well, do not pass any legislation for a while. Nothing, zero.

That is certainly an option, but probably not a very practical option in this political climate. So, we dismiss that option, whether it is meritorious or not. From a political point of view, the Congress will repsond to perceived problems. There will be some action taken.

I think my direction is to try to look at it in more of a macro approach rather than the micro approach we have taken in the past few years in legislation. What it comes down to is that nobody really wants to come up and say, well, this thing ought to be repealed.

The argument is that it is not bad legislation. The way it is written, it is ambiguous enough, but we do not like the way it is interpreted. There is a little hedging there. It is making it difficult on us.

I tell you what you are going to have to do. You understand the political sensitivity and the political situation around here. You will have to come forward at some time—business and industry—and show us that there is a $600 toilet seat that has been created by Congress and the Department of Defense.

You are going to have to give us your full story. You have to show how these regulations and laws are adding to the cost of doing business with the Government. You have to show how the life cycle of the program has increased by 2 or 3 years because of congressional laws, regulations that have been implemented by DOD.

That gets attention, that gets everybody's mind focusing in a direction. Until we do that, I think we are going to go back and forth, like Joe Theisman out there trying to duck a little bit and getting sacked six or seven times a game. I feel that we really have to be very precise.

We are going to have to come up with stories or going to have to come up with facts and statistics that show these things are not working. Otherwise, let us be quiet.

The bottom line is forging a consensus, and see where we can go and work with the Packard Commission.

I will just ask one question. That is: Are there laws there that simply ought to be repealed? Are there regulations that are not working and if so, give them to us?

You started with Public Law 98-525. We have to have specifics on why this is not good. We hear a lot of rumbles out there, but we have to narrow this thing down if we are going to try to make progress. I think the procurement legislation that was passed this year, took more of a macro approach, but there will be some perhaps repeals, modifications of things that we passed in the past.

Does anyone want to pick up on that point? Each of you might want to respond very quickly.

Mr. CLARK. I think your opening statement hit the nail on the head. Generally the problem is not absolutely with the legislation itself. It is with the interpretation and then with the overzealous implementation through regulations which squares the desire of the legislation in terms of its impact on the industry.

Data rights is a very good example. We understand the needs for data rights. We understand the intent of Congress. But when the regulations apply to commercial practices, to developments made with commercial funds not supported by any financing of DOD, it creates a lot of systemic problems.

You hit the nail on the head when the different members of the Department of Defense, the services, implement their own regulations instead of using the DAR method of getting the regulations out. We are responding to six different regulations on the same subject, none of which has continuity.

It is the implementation that is the serious nature of the problem. I do not know whether it is possible to consider more precise definitions or history in the record of legislation. I do not know how that is done, but that would, indeed, be helpful.

Senator QUAYLE. You have six different sets of regulations?

Mr. CLARK. The time gets critical. There are over 450 regulations changes pending in the DAR system now. That system is absolutely choked and clogged. When that happens and the law requires implementation by a certain date, then the services, the Army, Navy, Air Force, Defense Logistics Agency, and others, put their own regulations out and their perception of what the law requires.

So, we are responding to four, five, or six, in some cases, different interpretations of the same law. That is why in the closing part of my statement I suggest that the system is choked and more legislation on top of a choked system is going to cause increasing costs and problems associated with the acquisition system.

It was not made facetiously to try to get somebody to stop legislation. It is merely a step to get recognition that the system is in fact choked.

We are getting now multiple implementations in lieu of the precise disciplined method that the present system is designed to impose.

Mr. LIGHTNER. I agree with Mr. Clark. Actually the people are reinterpreting the old regulations and micromanaging in a way that is not in the old regulations. That is one of the things that is killing us.

I guarantee you your costs are going up an awful lot because of the reinterpretation of those regulations.

Senator QUAYLE. Give me examples of where regulations have cost us money. Cite the regulations.

Mr. LIGHTNER. DO 6553 which has now been changed to 1412. They require now a so-called consolidated bill of material. With that consolidated bill of material at times when we are bidding on line items of a bid where it is a shopping list for the customers, the DCAA will insist that we provide a consolidated bill of material for all the line items, which is a waste of money.

Senator QUAYLE. Let us put some figures in the record.

Mr. LIGHTNER. I am not prepared to put it in here, but we can put in numbers. We can tell you hours that are wasted.

Let me tell you another one. We are forced to use a standard cost system by one of our contracts. The old way of bidding jobs is when you take the guy, the machinist, that knew what it took, the hours to do the work. He bid that job because of his experience. Or the woman that does the assembly of a microelectronic piece of equipment. She would know what is necessary.

Now you must prepare paperwork to show why this is done, which gradually forces you into a costly standard cost system.

Further, with the standard cost system you've lost competitive advantages, and just about anybody can pick off the job. Incidentally, we have run cost on the standard cost system in one recent contract, and it is higher than our old cost system, but it is acceptable just because we have shown rationale.

Mr. HAHN. I would agree with all the witnesses we are choking on regulations right now. I do not think we would be if we had an efficient procurement system in the first place.

The problem is, Congress makes very sincere attempts to improve it, but the regulations that come out to implement that do not reflect the intention of Congress. I will give you an example.

In the tooling and machining industry, our private customers are Defense Department customers. We use a prequalification, if you will. It is simply a method of identifying companies who have the right equipment configurations to make a product.

It is not a method of quality control. A company can have a small lathe, medium-sized lathe or large lathe. You do not want to give a product to a company that does not have the right equipment to produce that part. There are 40 or 50 types of machine tools. A customer, whether private or commercial, can call us and say, "I have a print in front of me. I need a guy that has a medium-sized boring mill, a large lathe," and we can screen, using data base, the companies that have the right equipment configurations to produce that part. We have a computerized data base.

It is not quality control. Quality control is a statistical method applied afterward, sampling, testing, and measuring parts to make sure you are getting quality products. It is used by private industry and prime contractors.

We have offered to give it to DOD, but they will not take it, and the service branches, either for a prototype or supplement to their existing system. It could save them a heck of a lot of money. It could enable them to use sealed-bid competition and if you sealed bids, you do not need all these rules, the low bidder gets the job.

If he makes a lot of money, who cares. If he loses a lot on money, who cares. You can save yourself absolutely the most, not only in terms of paperwork and everything else, but in efficiencies if you can buy more of your goods and services by formally advertised sealed bid.

Yet the services, the procurement policymakers are not operating in a sensible business-like fashion.

Senator QUAYLE. Senator Levin?

Senator LEVIN. Mr. Hahn, you mentioned in your testimony a certain percentage of spare parts procurement which was openly competed. According to your statement, that is the way it reads. I think in your overall statement you said by formally advertised competition.

Will you modify that? The 10 percent figures that you used on page 4 of your statement relate to a bid process by publication.

Mr. HAHN. Formally advertised, either in Commerce Business Daily or posting it on bid boards. Some formal advertising, whether it is a sealed bid as opposed to a sole source or negotiation.

Senator LEVIN. Do you know what percentage of the spare-parts procurement is obtained through competitive negotiations?

Mr. HAHN. That figure is a hard one to get at. Unfortunately, the two figures, it is my understanding that they collapsed the two. I think that is a shame because our experience is that if you want to get the lowest price, make it a sealed bid purchase.

Senator LEVIN. Competitive negotiation can at least, at times, be truly competitive and appropriate. At other times it is not. Nevertheless, it would be useful if at least for reporting purposes we asked the DOD to tell us the percentage that is acceptable.

I did a change which I have been considering in the Competition in Contracting Act. We have now allowed them to consider competitive negotiations as competitive. I think there is good reason to do that because I think you can in fact be competitive, at least it would be useful to know what percentage of the competitive contracts are formally advertised and what percentage is negotiated even though they are treated the same for other purposes.

That is something that we are working on. It is a fairly small amendment to the Competition in Contract Act, but it would be useful.

Mr. Hahn, you have proposed that there be a new way of procuring. You suggest that we have an independent defense procurement agency. That is being discussed by some. There are pros and cons to that.

I wonder if our other witnessess will comment on that. Maybe they did in their statement, but I did not hear it orally.

Mr. Clark, are you familiar with that proposal and do you have any comment on it?

Mr. **Clark**. That is a long answer, Senator. The behavior of the Department of Defense in terms of controlling the process of defense procurement is fractionalized in that arena. We get different views from the different services. The proposal that NSIA has put forth suggests that it would be very wise to have clear authority and accountability by the Department of Defense at the Secretary of Defense level.

Delegations to the services result in some sense of abdication of control and that is in fact what is going on in the Department of Defense now. Those Service Secretaries are indeed responsible, and I am not questioning their responsibility. But, understanding the behavior of the Secretary of Defense, control of that process is now limited by its own structure.

So, we are advocates of a central policy authority specifically and precisely responsible and accountable for the entire procurement activity by all the Department of Defense. To that extent, we favor change but not an independent procurements agency.

Senator **Quayle**. Mr. Lightener?

Mr. **Lightner**. I have not thought much about it, but I have a tendency to disagree and think that the procurement activity should be not centralized, but I think it should be decentralized.

Senator **Levin**. I think it was Mr. Clark who testified to the question of the standard labor, the work measurement standard.

Mr. **Clark**. Yes, sir, I did.

Senator **Levin**. Are you familiar with the Senate and House bill which has been introduced to modify the language in that authorization bill, Senate bill 1783?

You will not know the number necessarily, but the bill I introduced in the Senate and a similar bill was introduced the next day in the House. It has passed the House.

It would modify the language in the authorization bill relative to the work measurement provisions. It would delay for 6 months in order to give us a chance to have hearings.

We are not at all happy with that language. It is a long story as to how it got there. At any rate, the chairman is not happy and I join his unhappiness totally in the process and the result. It will create a whole lot of paperwork in the Department of Defense.

At any rate, the bill would delay the implementation for 6 months to give us a chance to hold hearings. It would clarify the situation so that it would be clear if a contractor does not record that information, the DOD does not have to obtain it.

One of the problems with the language is that it at least, as read by the DOD, requires the DOD to obtain that information even if it is not kept by the contractor. It is a new burden and I think a very onerous burden, as a matter of fact.

The people in the House said such was not their intention. So, I introduced a bill to clarify the intention. But what the House would get out of this bill would be to apply the recording requirements to existing contracts where the contractor already records the information.

In other words, it would say if that information is kept by the contractor, then the DOD would obtain it on existing contracts, not just on future contracts. So, two of the three provisions are possible from our perspective.

One would be delay.

The second would be the clarification that the DOD would not have to obtain this information if the contractor does not already have it in his files.

The third would cut the other way slightly, the third part of this bill, in that it would say that where the information is kept on existing contracts, then the DOD would obtain that from the contractor.

Are you familiar with that bill?

Mr. CLARK. I am familiar with the implication. I am not familiar with the language, but let me say amen and add one parenthetical comment.

What is being imposed now on the industry is standard labor hour contract clauses. If you are desirous of being a low-cost producer, you need to tend toward automation. Automation takes labor out of the company. We have in our company products that are being produced by less than 5 percent direct labor hour content.

To impose that standard on that kind of product with that low direct labor, our content is creating a cost that is not going to solve anybody's problems. Having the flexibility to look at it intelligently from that standpoint, the answer is yes; I agree.

Senator LEVIN. Will you take a look at that language because we are interested in obtaining comments from industry on that language?

Mr. CLARK. I certainly will.

Senator LEVIN. Mr. Lightner, are you familiar with this bill which would modify the language that is in the authorization bill?

Mr. LIGHTNER. I am familiar with the type of costing you are talking about, but I am not acquainted with the bill. It seems to me for a bill of this nature that we should exempt the competitive contracts.

Senator LEVIN. They are exempt.

Mr. LIGHTNER. Where it is a negotiated contract?

Senator LEVIN. They are exempt.

The point is where a contractor keeps this information, whether it is competitive or not competitive is not the issue, then it should be available. That is the point. The problem with the language in the authorization bill is that it imposes a new requirement even where the contractor does not keep that information.

Where the contractor does not have that available, why do we want to require that?

Mr. LIGHTNER. They require all sorts of additional information that we do not think we need to manage our company.

Senator LEVIN. Would you take a look at S. 1783 and come back to us?

Mr. Hahn, are you familiar with that provision?

Mr. HAHN. We are somewhat familiar with it. We will be happy to give you our thoughts.

Basically, our members always bid competitively. If you have competitive bids, that retention of information is not required and it is irrelevant anyway.

We will be happy to suggest some ideas to you.

Senator LEVIN. I will join the chairman and the other members in soliciting from each of you for the record specific provisions in law or in regulation which you believe should be repealed. The more specific you are in your submission for the record, the more helpful it will be.

Thank you.

Senator QUAYLE. Senator Warner?

Senator WARNER. Thank you, Mr. Chairman.

I wish to commend the Chair and the distinguished ranking minority member for holding these hearings.

Since 1969 when I crossed the threshold of the Pentagon, I have observed it from different seats at different times.

I would like to ask Mr. Clark a question and feel free to say, "Senator, I prefer not to answer that question."

In my study, information and observing it for some 15-plus years, it seems to me we have come to the point where we have almost imposed de facto nationalization on the defense industry.

Would you comment?

Mr. CLARK. You bet I will. I will be delighted to comment. In our NSIA testimony before the Packard Commission, the President's commission on defense procurement, we raised that issue very strongly.

Senator WARNER. Using those words?

Mr. CLARK. Yes, sir. In fact, the words "nationalized industry" are specific to the testimony. It is meant to imply what is being regulated through the system is how to manage the enterprise. They are taking the accountability and management responsibility away from management by legislation and through the regulatory process.

I could cite you chapter and all kind of stories on that. I will be glad to submit examples.

Senator WARNER. That is interesting. I thought I had come up with an original.

Mr. CLARK. No; it is very real and it is very true. It is the Department of Defense's methodology of getting it from the regulatory process clear downstream to the people who are taking action. It is really a heck of an imposition.

We will submit things on audit. That is just one example. Ten percent of my administrative staff is just cost generation to be responsive to audits, the majority of which make no significant contribution to the process, the quality or the performance on the contract.

Senator WARNER. Consequently, the United States is experiencing the disadvantages of nationalization as such in inefficiencies and cost.

Mr. CLARK. One very serious result, and I mean this in the most flag-waving sense I can muster, what is happening to the process and all of the senior executives of the Department of Defense are very aware of this and complaining about it, the time and cost it takes to bring a major weapon system in the inventory in support of our defense needs now is sufficiently and significantly rather longer than it takes the Russians to do exactly the same thing.

Our lead times are terrible. If you have not seen it, and I do not know if it is proper to make this comment, you might want to listen to the Foreign Technology Division presentation of the comparison.

If I say any more, I will get into the classified arena.

Senator **WARNER**. Mr. Hahn?

Mr. **HAHN**. I would like to make a comment, if I may.

I am certainly sympathetic. We do overmanage and part of the reason we overmanage is that we buy so much, I believe 60 percent of the Defense Department procurements are sole source. As a result of that, there are all the horror stories you hear about, charges and overcharges. That brings regulations.

The other consequences in our segment of the industry are that by sole source procurement you about double the time of procurement. We believe if you use more competition, for every percent increase in competition, you can decrease by 1 percent the companies you have to regulate.

It is that much more efficient procurement, that much lower cost and that is a stronger defense and diversified defense industrial base.

Senator **QUAYLE**. Mr. Lightner?

Mr. **LIGHTNER**. There is something else that I am not sure you gentlemen are aware of. You are aware that the DOD is now dictating to us what salaries we can pay our people? We have been informed that they are going to disallow 13½ percent of our salaries and make them unallowable.

Senator **WARNER**. Unless we unravel this, Mr. Chairman and members of the committee, this country will have its R&D advantage and technological advantage snared in an option of delusion. That is one individual observation.

I commend the Chair for his efforts.

Senator **LEVIN**. Let me make one comment.

I tend to agree that we are becoming much too regulated and complicated. Mr. Hahn's basic point is if we have more competition, we do not get into the problem of regulation and we should not because the market regulates it for us. There will be areas where we cannot usefully have competition; we could save money. Mr. Hahn will acknowledge that. He will agree we could have a lot more than we have now. Industry will have to help us solve the problem of the perception that there are an awful lot of toilet seats, Allen wrenches, and so forth. I said this at the last hearing and I will repeat it very briefly.

Defense Daily captures it very well, and you might want to read my brilliant remarks in the November 8 edition of that paper, but industry ought to get together. There is not necessarily an agreement on this, by the way. There will have to be a way to address that perception quickly, no questions are asked when those kinds of issues come up because it is corrosive.

Public confidence in the way we procure is undermined seriously by the stories that have come out. We have got to address that. If we do not, we are going to see an undermining of defense in general. We are also going to see more regulation, and not less, because

Congress is likely to respond in some way. We may do it foolishly, illogically or brilliantly, but we will respond. When we respond, we will respond because there is no way not to when people read and hear what they have been reading and hearing.

I am not going to say it is not your responsibility. I do not want to shove it on your laps and shoulders because obviously we have to bear the ultimate responsibility, but I do think the industry ought to get together and address that perception in a very quick, no questions asked kind of way without going into a lot of details that I went into last time.

I am not sure my proposal is the right way, but the industry could be helpful to us in addressing this perception. Again, I refer you to at least that proposal made a week ago. If that does not answer it, give us some other.

Senator WARNER. I think the Senator from Michigan should be commended. His observation is correct. We tend to overreact.

Mr. Chairman, just one brief question here, two reasons, based on my own experience serving under three Secretaries of Defense, prepared by one of our staff.

One strong general feeling that I get from the statements this morning is that there is not adequate and timely dialog between the Department of Defense and the defense industry in the implementation process.

What steps can be taken to involve the industry and other affected parties at the front end of the rulemaking process without adversely affecting the need for timely implementation?

Each Secretary and his deputy have a different style. When I was there, it was pretty much of an open door. We had regular access with industry and all levels. Would any of you care to comment on that today?

Mr. CLARK. That is a very good point, Senator. We share the view, we think the 30-day rule for getting responses back is very important in this process. We intend to be responsive to it. We have proposed that a board of industrial persons be implemented into the system for observation, reaction and getting the recognition of what the imposition of a regulation would do so that it is carefully and thoughtfully worked out before it is imposed.

That system is not in process now because of my aforementioned jamming the FAR system with 450 regulations that cannot seem to get out of the system. It is very important that industry be heard. We want to be accountable. By being heard, we can best be accountable to what the intent of the Congress is.

Senator WARNER. I think the observation is well taken.

Mr. HAHN. We also suggest, among other considerations, we are very happy with the legislation passed last year that required Federal Register publication as a means of enhancing the ability of the business community, particularly the small business community, to see draft regulations.

Now we have a vehicle of seeing something before publication in their final form.

Another consideration might be a more careful attention to the Regulatory Flexibility Act. There generally does not seem to be such interest in looking very closely at the impact on small businesses of new proposed regulations.

We think that DOD ought to more closely pay attention to the requirements of that act and its implications and its impact on business.

Senator WARNER. Thank you, gentlemen.

Thank you, Mr. Chairman.

Senator QUAYLE. Thank you, Senator.

I thank the panel. We look forward to the submission of specifics you would like to see repealed in past laws or any laws that are presently being implemented or discussed. It will be helpful to us.

Our second panel, please come forward.

Mr. Lloyd Hallamore, director, SAN/BAR Corp.

Mr. John Toups, president and chief executive officer, Planning Research Corp., representing the Professional Services Council.

Mr. Hal Rosenbaum, president, Hal Rosenbaum Associates.

Mr. Cyrus P. Knowles, vice president, R&D Associates.

We have the light in operation.

Mr. Lloyd Hallamore, director of SAN/BAR Corp., is the first witness.

Welcome.

STATEMENT OF LLOYD G. HALLAMORE, DIRECTOR, SAN/BAR CORP.

Mr. HALLAMORE. Thank you.

You blew my whole pitch by the 5-minute rule.

I disagree with some of the comments that were made earlier. We are primarily in the innovation business, if you will. I started a little company 35 years ago. Thirty years ago we merged with another small company and we became a very large company.

So, I have spent a lot of time in small business and in large business. Now I am back in small business again. What I find is absolutely staggering to me when I see the difference in the procurement regulations and the implementation of those regulations in the 15 years or so since I was with a large organization.

What I am finding is that the implementation of the Competition in Contracting Act is so severe that sometimes, as I say in my written statement, sometimes I wonder whether we are dealing with the U.S. Government or some back alley counterfeiting shop.

The things that we do in our organization is to innovate. We support our product in the field and in so doing we recognize certain needed products and systems and then with our own money we go ahead and do this job and then present it to the military.

What we are finding now with the Competition in Contracting Act is that unsolicited proposals, which is a normal way of putting a new product into the inventory, is almost unacceptable. This I cannot believe.

I think that any innovative organization that recognizes the need by the military for a new product should be able to convert that spontaneous enthusiasm about that product into a little cash in the till by getting a contract and not give up its rights for competition until it at least has gotten its money back on its original innovative work and a profit besides.

This we are finding is not necessarily the case in some of the procurement agencies as they are implementing the Competition in Contracting Act.

Also, there is another situation I find almost possible to believe. That is reverse engineering for which some of the procurement people, particularly at lower level, not at the higher level where they recognize how things can be done, are in almost a circle-the-wagons mode. If you have a sole source item, they find it almost impossible to award you that sole source item without going out for competition.

We have one particular case at the present time which is a secure communications device. We are the sole source. We patented the product. We developed it with our own money. The buyer is currently saying he cannot procure without going out for competition.

All this is leading to is delay in production and delay in the acceptance of a needed item, but the strength of the competition advocacy program is such that it almost makes everybody tighten up and not move forward.

I believe that a change should be made in the implementation of the Competition in Contracting Act before it gets truly set in concrete, including the reverse engineering in the competition advocacy program where brownie points are awarded to people who can get the most competition.

Maybe there ought to be demerits awarded to the person in Government who holds up a procurement which could seriously affect the combat readiness of some of our units.

I see that yellow light is glowing at me.

All I can say, as far as I can see, it was not the intent of Congress to stop the procurement process cold, which is in some cases happening today. Maybe an expression of the intent of Congress would correct the way that the lower level procurement people are accepting their supposed responsibility for more competition.

Do not get me wrong. I am also against sin and for motherhood and for competition, but there are places where competition for competition's sake is not proper.

[The prepared statement of Mr. Hallamore follows:]

PREPARED STATEMENT BY LLOYD G. HALLAMORE, DIRECTOR, SAN/BAR CORP.

I guess that I should first qualify myself as somewhat competent to talk on the subject of Procurement Legislation passed last year. About thirty five years ago, I started a small company with very little money and four employees that primarily made things for the Military. That Hallamore Company grew rather rapidly and in 1955 it was merged with another small company called Siegler Corporation (some people could say we didn't merge, we traded overdrafts) and I operated as the Hallamore Electronics Division of the Siegler Corporation doing mostly engineering and production work under contract with Military agencies. That small Siegler Company, doing about 9 million a year, was the base from which a group of hard working people caused to become what is now Lear Siegler Inc., a company doing over 2 billion dollars in business per year.

After 15 years of working hard in helping in that growth - and when we had hit between 500 to 600 million in business, I retired in 1970 - and that was the worst 3 weeks in my life.

My son had started a business in 1962 which he named San/Bar Electronics - and after those miserable 3 weeks of retirement, my wife called my son to ask if he didn't have an office for me so she could get "that old goat out of my house".

So from being the Chief Honcho of a small business, I went on as Vice President of what became a very large business - back to a small business with the title of "Director" and "Executive Relative" but operating as "Director of Corporate Development".

In all the above, I was highly involved in Military Contracts and am quite proud of the work we did for the Military. As examples, Hallamore Electronics was one of the seven organizations given awards by the Secretary of the Army for "outstanding contributions" in getting our first satellite into orbit -- and when John Glenn took the first ride around the earth, we worked night and day to build tracking stations in vans that were placed around the globe to monitor his flight. The Hallamore TV Camera on the ECHO Project was the first tv camera into space and is now in the Smithsonian Institution. We built the Automatic Sequencing and Launch Control equipment on the Atlas ICBM Program for Astronautics in San Diego and the Air Force on a fixed price incentive contract, for which we got an award that states "Hallamore performed feats rarely witnessed even in these days when the difficult we do immediately, but the impossible takes a little longer".

I could go on and on because we were involved in nearly every missile and space program conceived - along with building other more down to earth equipment for the foot soldier and sailor.

My greatest concern in the interpretation of the Competition in the Contracting Act is that, as implemented, there will be a stifling of innovation by industry in trying to supply the Military with improved products. One result is an almost total shut-down of acceptance of Unsolicited Proposals.

Any company worth its salt supports its product in the field, whether it is Military or Commercial. In so doing, those companies will recognize possible needs for products or systems that would be more effective and useful to the User Agency. In the past, the normal method for converting that innovation into hardware was for the companies to make Unsolicited Proposals for contracts to provide those improved items to the Military - and that method worked.

However, now it seems that the Act is being interpreted by some agencies to almost require that, when a company on its own initiative recognizes an opportunity to help the Military with a new product or system - and spends its own money to develop that idea or hardware for presentation to the Military - then the Military agency must copy that new idea and send it to many other companies for competitive bids.

The effect of this could be the stifling of desire to innovate on the part of a company who has spent the time and money doing its homework -- only to find that some other company who had just sat still and had no prior investment in time or money in conceiving a new idea could naturally under bid on certain programs.

It should be obvious that a company which had spent its time and money to create a new item for use by the Military should at least have the opportunity to recover its costs and a profit before it releases its rights for competitive bidding. There are adequate safeguards in current procurement laws and regulations to assure that the government would get a fair deal in such a circumstance.

To illustrate some of the processes a company goes through to get a better product into the Military to help the Military in its missions, I think it best that I describe some innovations that San/Bar has created. I am speaking as a representative of a small company but having also been involved with operations of a large company, I can assure you that our small business concern with the new Competition in Contracting Actions is the same with large businesses -- except the large companies probably would have to add more zeros.

Several years ago, San/Bar completed development of a product for cleaning, lubricating and protecting from corrosion telephone dials and the product which we named "BREAK-FREE" worked beautifully. Using it on our own guns and fishing gear, it became apparent to us that this product could answer some real problems the Military had, particularly on the M-16 and large caliber weapons. We spent over three years and about $1.5 million dollars of our own money demonstrating "BREAK-FREE" to many Military agencies with firing tests in all types of climate. It was finally adopted as a Military standard because it did solve a lot of problems that were the cause of great concern in the Vietnam War.

In supporting our product in the field, we recognized another problem in the cleaning, lubricating and corrosion protection of large caliber weapons. Because of the efficacy of our "BREAK-FREE" product, we were able to develop a system, which we called "Bor-Cap" that enabled the gun crews to treat their weapons in one hour, as against a normal three day cleaning cycle, using one third the personnel and with greater safety to the crews. There was a great deal of interest in this system by the users - the people actually firing the weapons. Having developed that system on our own money and spending about two years of considerable effort on our part in testing and demonstrations, we presented an Unsolicited Proposal to the Army. Thank God, we made that proposal prior to the end of March 1985 because evidentally there was a magic date of 1 April 85 at which time Unsolicited Proposals were looked at as almost non-acceptable. We are currently manufacturing that system for the Army.

We also recognized that the soldier with an M-16 rifle had a problem. When he fell into water or mud, his cleaning equipment in the butt-well of his rifle became wet and dirty, making it difficult to properly clean, lubricate and preserve his weapon. We figured that if we made an airtight container for the cleaning kit that would fit in that same butt-well, it not only would help him in normal operations but would keep out chemical contaminants in an NBC atmosphere.

We developed and tooled such a kit at our own expense -- and we goofed -- because the seal was not adequate. In association with Tupperware, we then corrected the tooling and just this week have completed a kit with a Tupperware seal which is the best in the world. At no development expense to the government, we have a product that will answer the problems -- and the Military needs it -- but we are now faced with the problem of how do we get on contract to produce it without having our drawings sent to every outfit in the country who had invested nothing in the innovation, development and experimentation -- and who didn't have to recover those expenditures we made. Needless to say, we are working on the problem.

We have been told by some Military personnel that, under the new rules, we are in the same position as if we had developed a product for the consumer market and where we would take our chances in the market place. My answer is "In the consumer field, there are multiple potential customers, but when we developed a cleaning kit for 155mm Howitzers, we only had one customer because we don't know many people who have a Howitzer in their backyards."

However, we understand that now even products that have been developed for the commercial or special markets - and even where patents have been issued - are now being attacked by "Reverse Engineering" programs in certain agencies. An example is a telephone device San/Bar developed, patented and has sold for several years. An urgent requirement now exists for that item in a secure location, but the responsible buyer appears to be holding up procurement awaiting a possility of creating competition by Reverse Engineering that product. That will only lead to legal action and delays in getting the item to the using agency.

We are continuing to work on several developments that we believe can help the Military. When our development people come to me with an idea they are excited about and believe will work, I point to a prayer I have on my office wall which says:

> "Let us convert some of this spontaneous enthusiasm into a little cash in the till"

In other words, to keep up our enthusiasm and drive, we have to be able to get on contract so that funds are available to keep us in business.

We are also continuing our efforts in studying Military needs and, as an example, we reviewed the GAO report on the storage of large caliber ammunition. The problems described in that report seemed to us to be easily answered by proper containers for that ammo. But, we figured that if new containers should be built, then we should analyze what else that container could do to help the gun crews in the handling of the ammo and protection for the crews. We had just about completed our studies and were readying for an Unsolicited Proposal, when the Army came out with a Request For Proposal for 105mm containers to be made out of plastic.

We have responded to that RFP with a very complete technical proposal and we now just hope that some of the ideas we had that would help the gun crews, which we were preparing to put in an Unsolicited Proposal, are also being taken into consideration during the evaluation of that RFP.

In working with Tupperware, we recognized what could be certain definite benefits to the Military by making products using the Tupperware seal, particularly where certain Military items might be stored or used in an NBC environment. The Tupperware Company also showed us a dramatic new plastic on which they had recently completed their development work changing it from a laboratory item to a commercially producible product -- they call it "Xydar".

"Xydar" has been referred to in a well recognized periodical as "an introductory product whose extraordinary potentials spell a materials evolution even more sweeping than that from iron to steel". Dart & Kraft, through its Tupperware and Dartco subsidaries has spent many millions of dollars in the development of that product and has also spent many millions more in building a plant and laboratory in Augusta, Georgia - and, we understand, are prepared to spend more in the expansion of that Georgia facility as the demand warrants.

Tupperware has recently introduced that product to the consumer field under the name "Ultra 21" and is making and selling a series of cooking utensils that can be in a deep freeze - put right into a high heat oven - thrown to the floor without breaking - and last a lifetime. When I first saw that product, my only thought was "the Military needs that for many purposes".

"Xydar" is truly amazing in that it is injection moldable - as strong as metal - light weight and will not burn in a normal atmosphere. Burning can be achieved in the laboratory with approximately 50% oxygen -- but even then, there are no toxic fumes. The output from burning is water (steam) and carbon dioxide.

It doesn't take much imagination to recognize the Military potentials for that plastic. Consider the possibility of an interior of an aircraft where there is a great deal of plastic which, with current materials, throw off very toxic fumes when burning in normal atmosphere (about 21% oxygen). Maybe some of us who ride a lot of airplanes could even help save ourselves if we got this product into use at the earliest possible moment -- because a lot of people have died in aircraft crashes from toxic fumes of burning regular plastics.

Or, consider the potential benefits to the Army in its "Lightening of the Forces" program -- whereby great amounts of money could be saved in transportation - and containers that would not burn for storage of artillery ammo - and to the Navy in being able to use aboard ship light weight plastics that won't burn. I could go on and on, but needless to say, San/Bar through its BREAK-FREE Division, has a great interest in furthering the use of Xydar by the Military and has made an arrangement with Tupperware and its Dartco affiliate to find Military end-product uses. We are working with several Military Agencies and those Agencies have shown a great deal of interest and we expect to expand our efforts with them -- but up crops the bugaboo of the Competition in Contracting Act.

We believe that this "Xydar" program should qualify under exemptions stated in the Competition in Contracting Act -- but we have concern that some lower level contracting personnel, under the program whereby contracting agencies seem to get "brownie points" if competition can be achieved, might unnecessarily extend the time span for introduction of new, highly desireable products for Military use. Maybe, if "brownie points" are awarded for proper competition, then "demerits" should be issued for unnecessary development time extensions by insisting on competition for competition's sake.

To conclude, I am not politically adept enough to know how some of the problems created by the Competition in Contracting and other Acts can be corrected ~~-- whether~~ by another Act - or an expression of the intent of Congress in passing the Act.

I know you have heard this before, but I will say it anyway, I think that Congress should act like a Board of Directors in a commercial corporation. That is, the Directors don't pass resolutions telling employees how to go to the toilet -- they appoint the management personnel, approve the business programs and provide funds to implement those programs. The day-to-day operations are left up to the management personnel - and if those people don't perform, then they are replaced.

It would seem to me that Congress should act in the same way - because, regardless of what the media may say from time to time, you have a great number of competent, dedicated managers in the Military Procurement Agencies - but when their hands are tied by actions of the Congress such as the Competition in Contracting Act - they seem to go into a "circle the wagons" mode and some necessary programs could grind to a halt. There also are thousands of people in industry who are equally dedicated to producing equipment on time at the lowest possible cost.

However, I am not naive enough to think that major changes in contracting procedures, which have developed over many years with greater and greater Micro-Management by Congress of Military programs, can be made overnight, if ever. But I do believe some of the bad effects of the recent Competition in Contracting Act can be changed before it gets "set in concrete" so that innovation by industry is not stifled. I particularly refer to the new handling of Unsolicited Proposals where industry could sometimes wonder whether they were dealing with the U.S. Government or "some back alley counterfeiting shop".

It seems to me that laws currently in effect are available to control any possible abuses - and they should be aggressively used -- but more freedom should be given to the contracting agencies than is shown in the Act. Again, don't require competition for competition's sake -- this adversely affects the availability of parts and equipment and could reduce Combat Readiness.

Senator **QUAYLE**. Thank you, Mr. Hallamore.

John Toups, president and chief executive officer of Planning Research Corp., representing the Professional Services Council.

Mr. Toups, please proceed.

STATEMENT OF JOHN TOUPS, PRESIDENT AND CHIEF EXECUTIVE OFFICER, PLANNING RESEARCH CORP. (REPRESENTING THE PROFESSIONAL SERVICES COUNCIL)

Mr. **TOUPS**. Thank you, Mr. Chairman.

I want to address my remarks solely to the question of what I believe to be the Government's failure to give due consideration to quality when it procures professional and technical services and suggest some ways to improve that.

The Government procures about $25 billion of technical services. Most of what has been said by the other witnesses, which is largley hardware oriented, largely applies to the service sector. There are a couple of differences I would like to point out.

First of all, unlike hardware which usually can be specified in reasonably accurate physical or functional terms, services are frequently very difficult to specify with precision before the fact, that is, before performance of the service.

Second, the quality of the service sought and ultimately rendered is often more critical in a service procurement than in a hardware procurement because service contractors are frequently hired to conceive, evaluate, test, modify, whatever it is, the weapon system or other hardware procurement.

Therefore, they can have a very leveraged effect on the cost and effectiveness of these other systems.

I believe there is really one overriding reason why Government fails to give due consideration to quality. It is a little bit like Mr. Hallamore was saying. The real reason is the environment in which the procurement process is taking place, characterized by mistrust on the part of three principal players, Congress, the executive branch and industry.

It has resulted in all of us being characterized very adversely by the media; with Government employees being pictured as dumb or lazy, Congress as inept, and me as a crook. I do not think that is very good. We all react to this one way or another.

The result is that we have hamstrung Government managers by tying them up with too many rules and regulations and thus preventing their exercise of professional judgment, which is the very thing they are being paid to do.

The product of Professional Services Council is output of human capability, technical expertise, innovative skills. We do not manufacture a physical product which can be objectively specified and evaluated prior to its purchase.

When the Government manager procures professional services, he or she must exercise especially difficult judgments.

First, the quality of the performance required under the prospective contract.

And, second, the ability of the proposing contractors to deliver that required quality.

In addition, there must be a balancing of cost, delivery deadlines, reliability and other quality considerations.

This also requires an environment where managers are allowed to manage and to properly weigh the various trade-offs of risks in the trade-offs. These risks cannot be eliminated. They cannot be legislated. They cannot be regulated. They can only be managed.

The current process discourages the exercise of judgment and, therefore, results in the arbitrary dominance of cost over quality.

A few thoughts on what we can do about them.

First of all, I do not think we need new legislation or any piecemeal quick fixes. I think Congress should work to stimulate fundamental improvement in the environment which itself will cause better implementation of current laws and lead to a more effective procurement process.

Second, I think the executive branch should move forward aggressively in the type of approach embodied in OMB's proposal called SCAT which stands for Simplified Competitive Acquisition Technique.

This proposal has the potential to reduce regulatory burden, improve quality and save time and money.

Finally, obviously, industry has to play a part in all of this. We have to work harder and be involved in the process. We have to rise above our self-interest. We have to be candid with our views on things. We have to basically support DOD's objective to move away from defining requirements in minimally acceptable terms to a system that will provide the best quality at an acceptable price as a recognized objective.

For us to do otherwise is national suicide. We cannot beat our enemies on the basis of more funds and more soldiers. We have to beat them on the basis of quality and sooner, not later.

Thank you.

[The prepared statement of Mr. Toups follows:]

PREPARED TESTIMONY OF JOHN TOUPS, CHAIRMAN AND CEO PLANNING RESEARCH CORP., AND PRESIDENT PROFESSIONAL SERVICES COUNCIL

Mr. Chairman and members of the committee, My name is John Toups. Today, I'm going to discuss our government's failure to give due consideration to quality when it procures professional and technical services.

I will voice this concern as President of the Professional Services Council (PSC), a trade association which represents the professional and technical services sector. Federal purchases of professional and technical services are estimated to be in excess of $25 billion.

I am also speaking as Chairman and CEO of Planning Research Corporation, a New York Stock Exchange-listed corporation with sales approaching the half-billion dollar mark. We are a technology-based professional services company with corporate headquarters in McLean, Virginia, employing over 7,000 people.

A number of the previous witnesses have addressed issues related to hardware procurement. Many of those issues apply equally to services procurement. There are, however, two extremely important distinctions which form the background of much of what I will say today.

First, unlike hardware procurement which can be specified in reasonably accurate physical and functional terms, services are frequently very difficult to specify with precision before the fact.

Secondly, the quality of service sought (and ultimately rendered) is often more critical than in a hardware procurement since service contractors are frequently engaged to conceive, evaluate, test or modify weapons or other hardware systems and therefore they have a direct impact on the cost and effectiveness of these systems.

There is one overriding reason why our government fails to give due consideration to quality in the procurement of services. That reason is the environment in which the procurement process takes place. It is an environment characterized by mistrust on the part of the three principal players: Congress, the Executive Branch, and Industry:

1. The Executive Branch has mismanaged the procurement process so that the process itself has displaced professional judgment; and
2. Congress has assumed a "micro-management" role when its proper role is one of oversight;
3. Industry has failed to strongly voice constructive alternatives to deal with a system which we know is inherently flawed.

We have all been a part of this problem. We now must work together to solve it. As we go about that task I believe one thing will become especially clear: we have undervalued the worth of professional judgment.

We have hamstrung government managers by tying them up with too many rules and regulations, thereby preventing the exercise of judgment. This is especially true in the procurement of professional services.

To make this point, I want to briefly review the basic characteristics of professional services.

In its most simple terms, professional and technical services is the utilization of brainpower to solve complex problems.

The product of professional services companies is the output of human intellectual capabilities, technical expertise, creative and innovative skills. We do not manufacture a physical product which can be objectively specified, tested and evaluated prior to its purchase. For example:

Professional services does not include the people who work on the assembly line producing a new tank, but it does include the people involved in all phases of the tank's life cycle: those who helped define why the tank was needed, how much the tank should cost through its life cycle, specifying the criteria for evaluating how the tank performs in battle and helping develop battlefield tactics.

Professional services does not include the people who work at "wet benches" in which wafers of silicon are dipped in acid and etched with patterns to transform them into microprocessors, but it does include the people who integrate hardware and software systems to create new and improved capabilities.

The professional services industry does not include the people responsible for making strategic military decisions, but people in our industry assist military managers in conceiving, acquiring and effectively utilizing sophisticated command, control and communications systems.

In such instances, the "product" being contracted for is exclusively the output of human intellectual and technical expertise. Therefore, when the government manager procures such services he or she must exercise professional judgment relating to the "quality" that can be expected from the proposing companies in addition to their quantifiable costs.

In other words, the acquisition of professional services must involve balancing cost and quality considerations—a "balancing act" which requires an environment where professional managers are allowed to manage professionally. The procurement of these services is ultimately a process of weighing risks and determining their relative importance. For example:

(1) The government manager must weigh whether choosing the lowest-cost contractor will sacrifice quality to the degree that life-cycle costs will be higher than anticipated; and

(2) The government manager must also consider the degree to which choosing the lowest cost contractor will increase the probability that a system (or effort) will fail to meet critical performance objectives; and

(3) The government manager must weigh the risk of whether choosing the lowest cost contractor significantly increases the probability of missing critical time deadlines.

These risks cannot be eliminated; they cannot be legislated or regulated—they can only be managed. But instead of understanding this basic principle, the current process discourages the exercise of professional judgment and thereby dictates the dominance of cost over quality.

Rather than understanding that in each procurement the government manager must evaluate critical trade-offs among performance, cost, time and other measures, the current process unduly curtails the freedom a manger needs to make these evaluations. In this environment, one who seeks to exercise good judgment may be putting his or her career in jeopardy.

How can we work together to change this environment? I said earlier that each of the three "major players" contributed to the problem. Now I want to suggest how each of us can contribute to the solution.

First, Congress should use the authority established by the Competition in contracting Act (CICA and other procurement legislation to aggressively conduct oversight hearings into the fundamental improvements needed in the system. In this process, you should avoid beginning with the unjustified presumption, which unfortunately the average citizen receives in vivid terms from the media, that all government managers are inept or that all those companies doing business with the government are out to "rip off" the taxpayer.

Rather, I believe you should use such hearings to acquire an understanding of what comprises professional services, and an understanding of the discretion required when government managers procure such services. Given an appreciation of the uniqueness of this situation, it will be evident that what is needed is not new legislation nor "quick fixes", but a new approach to result in a fundamentally different procurement process.

Secondly, the Executive Branch should move forward aggressively in the type of approach embodied in the OMB's Office of Federal Procurement Policy proposal for Simplified Competitive Acquisition Technique (SCAT). This proposal has the potential of reducing regulatory burden, and saving time and money.

While not a universal solution, it is a positive and fundamental initiative for improvement. The Professional Services Council (PSC) endorses SCAT and is working with OMB to insure that proper recognition of the "quality factor" is achieved. Our specific recommendations are included with our submission for the record.

Finally, industry's involvement cannot stop with a series of five- and ten-minute presentations to this Subcommittee. We must be an integral part of the process of finding better ways to fundamentally improve the procurement process. In so doing, we must exercise candor and rise above self-interests. At the same time, we must do our part to respond to what Assistant Secretary of Defense James P. Made told this Subcommittee:

"This concept of minimal quality must be replaced with a philosophy of continuous quality improvement. In DoD acquisition, competition is too frequently based just on price, and an 'award to the low bidder' mentality is too pervasive. As long as this persists, there is no reason for contractors to make quality improvement a way of life."

Finally, I sincerely believe that initiatives incorporating constructive and fundamental change are essential in our rapidly evolving world, and must continue with a maximum cooperative effort by the Congress, the Executive Branch and the private sector—particularly as it relates to the increasingly significant professional services sector.

ATTACHMENT A.—A PLAN TO IMPROVE THE PROCUREMENT OF PROFESSIONAL SERVICES

PSC believes that procurement of technical and professional services is a sufficiently unique area of Federal procurement activity to warrant a specific procurement process. The Simplified Competititve Acquisition Technique (SCAT) developed by the office of Federal Procurement Policy in the Office of Management and Budget provides a good framework and foundation for such a process. As currently proposed, SCAT has many advantages over the current system. SCAT will:

Centralize authority.—The contracting officer would be ultimately responsible for the procurement in all respects.

Shorten procurement times.—It is estimated SCAT will reduce the length of the current procurement cycle from 12-24 months to 70-85 days.

Cut contractor proposal bid costs.—By limiting technical proposals to 20 pages, cost of proposal preparation are reduced and savings result for the contractor and the Government.

More precise work statements.—Clear, concise, explicit statements of work will be prepared by the program officer and carefully refined.

Proceed along predictable award schedules.—The specific schedule for the entire procurement cycle will be included in the CBD notice.

Limit negotiations.—Award may be based on offers, as submitted. If a competitive range is established, one discussion per offeror will be completed in a week and followed by a best and final offer of not to exceed four pages.

Limit evaluation criteria.—Without deviation, evaluations would be made according to explicit criteria (including the specific quantitative weights assigned) set forth in the RFP.

While SCAT offers many advantages over the current system, PSC believes that it is necessary to refine SCAT by including a specific methodology for evaluating professional services proposals which gives proper recognition to quality.

This evaluation scheme, proposed as an enhancement to the SCAT, would consist of the following elements:

Requests for proposals would specify the relative quantitative weighting of the technical proposal and of the cost proposal and set forth formula by which technical and cost scoring would be performed.

A standard array of evaluation factors would be applied to technical and cost scoring.

In evaluating technical proposals, special weight would be given to the quality and relevance of past performance, as well as personnel qualifications, and innovation/creativity.

Technical and cost proposals would be scored using a standard set of qualitative ratings (e.g., good, excellent) and associated numeric score ranges. This approach will help eliminate the undesirable and artificially tight clustering of numeric scores often referred to as "technical leveling."

Technical proposals would be evaluted by the technical team with ambiguities specifically noted.

Clarification of technical proposals, if required, would be sought and totally resolved prior to scoring technical proposals. Scores would then be determined by the technical team without reference to the cost proposals, and sealed.

Once sealed, there would be no further discussions of the technical proposals and no further changes to technical scores. Based on these scores, the contracting officer would establish the competitive range.

Cost proposals would then be opened and scored for those whose technical proposals were judged to be in the competitive range. Special weight would be given to cost realism in scoring cost proposals with particular emphasis on the realism of proposed labor rates as compared to the actual salaries of resumes submitted. Program personnel familiar with the technical requirement would be included on the cost proposal evaluation team.

To prevent "buy-ins" to the maximum extent practicable, whenever a high level of quality is sought, the total weight of cost in the evaluation criteria should range from a low of 10 points to no higher than 30 points in a total 100 point system.

It should be noted that SCAT, as proposed, is limited to contracts of $5 million and under. PSC believes that the advantages of SCAT should be realized for contracts with annual value (i.e., revenue) of $20 million and under.

SCAT, with these enhancements, will produce an efficient and effective contracting method for professional and technical services. The SCAT methodology represents a return to basic contracting principles. Program officials are given greater input and involvement in the process with final authority for award selection vested in the contracting officer. Competitive emphasis would be placed on the quality of technical proposals, not on "low-ball" prices. The process is accelerated by limiting the number of iterations with the Government, by tighter submission and evaluation time frames and a less cumbersome process. Most importantly, a proper emphasis on quality of performance offers the prospect of real (not illusory) savings.

As with any new system, this alternative approach will work only if staffed by motivated, highly qualified, and well trained personnel. In the final analysis, SCAT, as modified, represents a major improvement opportunity for the procurement of professional services.

Senator **Quayle**. Thank you very much.

Dr. Rosenbaum, president of Harold Rosenbaum Associates.

STATEMENT OF DR. HAROLD ROSENBAUM, PRESIDENT, HAROLD ROSENBAUM ASSOCIATES

Mr. **Rosenbaum**. Thank you, Mr. Chairman.

I have a prepared statement which I include for the record.

I will restrict my comments to the tech base. Let me define for you what I mean by the tech base and why, in my opinion, the provisions of the Competition in Contracting Act are having a disastrous effect on that small, but highly important area.

The tech base is what we generally refer to as those line items that fall within 6.1 to 6.3a. It represents maybe 1 to 2 percent in terms of overall dollars of the total defense authorization. It represents perhaps the most significant part of the defense budget in terms of the future direction that the country is going to take. It supports the research, the innovation, it is the heart and soul of everything this country does to create a better defense structure.

What CICA has done is to apply procurement laws appropriate to defense hardware broadly across the entire defense spectrum including the tech base.

Let me make a simple analogy to show why different rules have to apply to the tech base. In my own life if I were to go out and buy an automobile, it is very clear to me how I go about doing that. It has taken me a while to learn, but now I understand how to do that.

I decide the kind of car I want and the options I want on the car, and I put the specifications down on a piece of paper, I put it in an envelope and mail it to six or seven automobile dealers. I ask them for their lowest bid because it is clear to me the only difference between buying a Ford from company A or company B is the price I am going to be charged.

When I go look for professional services like a doctor or a lawyer, I go about the process in an entirely different way. When I need surgery, I do not look for the cheapest doctor. I do not think you want the country to look for the cheapest scientist when you are spending money on professional services of that nature.

That is exactly what CICA is forcing. It is removing the authority of the people that you have given approval to, the guardians of the tech base, from deciding who it is they want to do "brain surgery" on the defense budget, who it is they want to come up with new ideas and concepts.

You are taking away from these appointed officials the ability to do what we call sole searching. Your are taking away from them the ability to use their judgment to go out into the countryside and pick the people they want to pick, with a few major exceptions.

For reasons that I cannot understand, CICA exempts institutions like the FCRC's from this restriction of sole searching. For some reason, a bureaucratic structure like CNA, Mitre or Aerospace Corp., that does not work for profit is exempt from the restrictions of competitive bidding. I personally do not understand that.

I have many friends and colleagues who work for companies like that. They are fine people and they do good work, but by no stretch of the imagination is all the talent of this country centered in Government laboratories and FCRC's.

Senator Warner talked about nationalizing the defense industry. That is what CICA is doing to the tech base, it is nationalizing it. It is taking small businessmen with innovative ideas, experts who wish to work in their own environment, and it is pushing them toward a system of supporting national laboratories or supporting larger companies. It is having a very bad effect on the tech base.

The same thing is true for innovation. My colleagues have talked enough about that. It is past the point where you can come in with an innovative idea and get encouragement to develop an unsolicited proposal to carry out the concept of that innovation, again with one major exception.

For some reason, the universities under basic research support have gotten that exception.

The yellow light has gone on. Let me tell you what my suggestions are.

I would like to see the tech base from 6.1 to 6.3a exempt from CICA.

Barring that, I would like to see basic research redefined to cover 6.1, 6.2, and 6.3a so that Government can buy under the concept of broad area needs.

I would like to see the same privileges that not for profit organizations like the laboratories and FCRC's afforded to other business entities like small businesses and other places where quality work is being done.

Thank you.

[The prepared statement of Dr. Rosenbaum follows:]

PREPARED STATEMENT OF DR. HAROLD ROSENBAUM, PRESIDENT, HAROLD ROSENBAUM ASSOCIATES, INC. (H.R.A.)

Mr. Chairman and members of the committee: Thank you for affording me the opportunity to speak today about the complications involved in procuring and providing defense research and development services under the provisions of the Competition in Contracting Act, (CICA).

Let me introduce myself to the committee. My name is Harold Rosenbaum. I am the President of H.R.A., Inc., a small defense systems analysis company that I started about eight years ago. At HRA we provide what is known as "expert services" to the Department of Defense. In addition to my duties at HRA I am a member of the Defense Science Board, (DSB), the Naval Research Advisory Committee, (NRAC), and a consultant to the Office of the Secretary of Defense. I have had experience working in large, hardware producing defense companies and had the opportunity to be a professional staff member of the House Armed Services Committee through Congressional Science and Engineering fellowship program. I relate this background to you because what I have learned in these varied positions has helped form the substance of what I would like to talk about today.

The problems involved in defense procurement are familiar to all of us. Many committees like this have taken and will continue to take testimony on abuses in the defense procurement process. The newspapers continually remind the public and the Department of Defense of mistakes made in the procurement of expensive military hardware. I am not here to either defend or condemn the military-industrial complex. I might only say that in my opinion there is enough blame to go around at least twice amongst all the participants, industry and government, and I wish we would get about fixing the problem instead of just finding scapegoats.

One of the ways that the government has chosen to fix the problem is through the provisions of the Competition in Contracting Act, (CICA). I wish to address the problems that act is causing to the part of the defense community that I represent, namely the research part.

An important part of the RDT&E budget is contained in the line item categories referred to as 6.1, 6.2, and 6.3a; categories members of this Committee are familiar with. What might not be apparent to everybody is the scope of this research effort, its unique nature and the importance it has to our overall national defense. First, the research budget (and here and for the rest of my discussion I mean 6.1–6.3a when I say research) amounts to only 1 to 1.5 percent of the entire defense budget. However, it is perhaps the most important part of the budget in terms of its effect on the future capability of the U.S. military establishment. If I may be permitted to use the simple analogy of a garden, research is like the seed used to grow the crops which in this analogy are the weapons we procure.

In our desire to insure that we use the most cost effective means at our disposal to buy the weapons we need we have applied a blanket procurement policy on weapons and research alike. We have said that we will buy the least costly F-15 or M-1 that meets the specifications that we took ten years or so to develop. Unfortunately we then also say that we will buy the least costly R&D, a quantity that is virtually impossible to define. In my simply garden analogy it is like saying—buy the cheapest seed that is labeled potatoes if potatoes is the product you want. Expensive seeds may often be the best buy. The seed, like our research budget, is an almost insignificant part of the total cost of growing potatoes. The most cost effective way to insure a bumper crop of potatoes is to buy the best seeds.

The Competition in Contracting Act, CICA, which may be appropriate for the procurement of hardware systems is having any number of adverse effects on the procurement of and the providing of research services to the Department of Defense. To understand why it is first necessary to understand the unique nature of defense research.

For the most part, research is a labor intensive activity. With little exception the government is buying labor hours not hardware products when it buys research. The nature of our defense business is such that labor hours are controlled by strict accounting standards that require constant auditing and approval of the cost of different labor categories and the techniques used to monitor who spends how much time on any one subject. Dollar cost, the discriminant in the procurement of hardware, is thus of secondary importance in the procurement of research. If the government requires the services of a senior scientists the cost of those services varies only within the narrow guidelines allowed for the particular expertise in question. By making cost the discriminant, as CICA does, the government guarantees it gets the cheapest scientist. It is like buying the cheapest seed for your garden or using the cheapest brain surgeon to operate on your tumor. It is nothing short of dumb and is the current way we buy research services.

It is easy to suggest regulations which downgrade the importance of cost in the procurement of research services. However, as long as cost is used as the figure of merit in the choice of all research services, the pressures to choose on cost alone, rather than more judgmental and thus less defensible discriminants like experience and capability, will always exist and eventually dominate the procurement system. There will be irresistable pressures to buy on price rather than quality. There are many research services where cost has no place in the choice of the best provider.

Another unique feature of research is innovation. The fact that we field the most technically advanced weapons systems in the world is the result of the incredible fertility of our technology base. We are the most innovative group of people in the world. Tragically, today there is little to no place for innovation in research because of CICA. In the past when researchers like myself came up with what we thought was a brillant idea there was an outlet for our energies. I wouild take my idea to the appropriate defense agency and submit it to the scrutiny of their experts. If they agreed that my idea had potential I could expect a research contract to develop my concept and see if it indeed was as good as I thought it might be. I don't have to remind you gentlemen of how many of today's weapons, weapons we had before our adversaries had them, were born of such a process.

Under CICA that process no longer exists except in some small and stylized ways. The most productive part of the defense research community, that part working in the free, competitive marketplace, is no longer able to secure support for innovative ideas. Any good ideas are, because of the way CICA is implemented, disclosed to everyone and then put through a process of competition to secure the cheapest talent to work on them; not a very comforting thought. People like myself are no longer anxious to discuss new ideas with our counterparts in the DoD. Within the DoD, consciencious program managers aware of new approaches to solve problems they have are frustrated by their inability to secure the services they need and thus to perform their jobs. It is no longer sufficient for them to be aware of the solution and have the necessary money to fund its development. They must now fight a procurement process that demands they take the extraordinary and costly steps of competing for a provider with no assurance that they will get the provider they want.

Research contracts have in the past provided the breeding ground for small companies. It is a well known fact that a large percentage of new ideas are developed in small companies that are not burdened by the bureaucratic constraints often present in big companies. Scientists and engineers often leave what they believe to be the restrictive atmosphere of a large company and start a new enterprise with new and innovative ideas. It is the great American success story. It might surprise you to learn that CICA is the bigest threat to hit small companies since I have been in business. My business has been what we in the industry refer to as sole source business. I offer a unique product to the people who buy my services. I give them fresh ideas on how to approach their problems, develop new and innovative concepts for them, and develop strategic frameworks for them to evaluate the country's defense needs.

Other small companies like mine develop new concepts whose successful development may result in better weapons systems. We are being put out of business because of the provisions of CICA. We cannot compete with large companies who can afford to put more people to work on answering any given RFP than we have in our entire companies. We cannot compete when our innovative ideas and concepts are distributed to large outfits, populated by a cheaper labor grade than ours. In short the only future for small companies under CICA is to be swallowed up by large companies or to front for them on those defense procurements that come out as small business set-asides. Paradoxically, CICA designed to reduce costs through increased competition, is having exactly the reverse effect in the research community. It is reducing competition by putting the largest segment of new competitors, namely small companies, out of business.

The other half of the government-industry research team is also being damaged. Government agencies are no longer able to procure the services they need. The procurement of any service is taking an extraordinary amount of time and energy and the entire system is becoming unnecessarily clogged. To make matters worse government agencies are turning to bundled procurements wherein a single procurement is used to fund services for three to five years. For the most part these procurements are more easily won by the larger service companies assuring that small business will be completely stamped out. Innovative research, often providing the solution to many defense agency problems is no longer a factor since it cannot be procured as such.

Government defense agencies very often require the services of specific experts. These involve an individual or a team of people led by a few well known experts. I should come as no surprise to anyone that the smartest people are not all within the Government. After all there is an incentive in our society, one we are quite proud and protective of, to be capitalists. CICA in effect denies the government the service of some of the very people it needs to solve what have to be the most complex problems of our times. In defense we sometimes address, especially at the conceptual levels dealt with in research, issues that may affect our very existence, e.g., nuclear war. To deny the country the opportunity to engage the best talent it has on these complex and important issues and to do so in the name of increasing competition is to me incomprehensible; and that is the kindest way I can describe such a decision.

There is a category of research "companies" exempt from many of the provisions of CICA. These are the "not-for-profits" and the universities. National laboratories, federally contracted research agencies, FCRC's etc., are permitted to receive government money without the need to compete. For some reason the fact that they earn no profit, in a country whose economic structure is capitalism, exempts them from the contricting requirements of CICA. There are many fine engineers and scientists working in the not-for-profits in this country. By no means, by no stretch of the imagination, do they or should they represent the sum total of technology talent this country has and must use to maintain its national security. The treatment the "not-for-profits" receive, i.e., exemption from CICA is not wrong. In fact it is so right that the answer is to extend that treatment to all research activities. That is, research as I have defined it, 6.1–6.3a should be exempt from the provisions of CICA.

As a member of the Naval Research Advisory Committee I recently headed a Laboratory Review Study Team. At that time the Navy Labs had been under what was known as industrial funding. Industrial funding meant that the labs had to compete amongst each other, program by program, and line item by line item. Of course this was not real competition for all the reasons I mentioned previously about the labor intensive nature of the entire research process. However, the Labs had to go through the motions, a process which resulted in an almost insignificant redistribution amongst them of the fixed research budget. What was significant however was the effect this was having on the entire sytem. In our review we found that laboratory bench scientists, instead of staying in the labs and working, were forced to spend more than half of their time marketing or competing for their funds. On the other side a bureaucratic structure within the Navy System Commands was created in order to be marketed. Our review team estimated that there was at least one monitor in the system commands for each 2 million dollars of research money; an incredible ratio. Whether as a result of our study or not, the Secretary of the Navy has recently moved to correct this situation. The labs will be block funded and managers of the tech base held responsible for assuring the research efforts are directed towards achieving the goals of the Navy.

I might also add that at the request of the head of contracting at the Office of Naval Research and some members of the Naval Research Advisory Committee like myself, the NRAC will most likely study the problem of research contracting for the Secretary of the Navy. We are all aware, those of us in industry and those of us in government, that we have a problem in the administration of our precious research funds. We are looking for answers that don't offend an already sensitive public. We need to be a bit bolder than we have been and explain to the public what is so unique and important about the defense research program.

Mr. Chairman, we need your help. We need you to understand that research, 6.1-6.3a, is very different from other parts of the defense budget. We know there have been abuses in the research programs as there have been in other programs and can only promise to help stamp them out. We don't think these abuses are anything but a very small part of the total effort and can't believe that to cure them you mean to damage the entire system. We need you to convey this message to the Department of Defense.

DOD officials have been under siege, through the newspapers and through congressional inquiries, and for the small dollars involved in the R&D programs are not encouraged to request these programs be exempt from CICA. There are probably many regulations that could be invoked to help alleviate the problems I have described. The fact is, however, R&D is different enough to warrant its exclusion from the provisions of CICA and I beseech you to support such legislation.

Thank you.

DESCRIPTION OF DOD RESEARCH AND DEVELOPMENT CATEGORIES

Category 6.1, Research: Includes all scientific study and experimentation to increase the knowledge and understanding of scientific fields related to national security needs. Such fields encompass the physical, engineering, environmental and life sciences. Category 6.1 efforts provide fundamental knowledge for solution of military problems that are addressed more specifically in exploratory, advanced, and engineering development.

Category 6.2, Exploratory Development: Those efforts directed toward solution of specific military problems, but falling short of major development programs. Activities vary from fairly fundamental applied research to sophisticated breadboard hardware, study, programming, and planning. The dominant characteristic of this category is that it seeks to apply new ideas, innovations, and technology to the solution of specific military problem areas. The feasibility and practicality of proposed solutions are fundamental to the efforts of the category.

Category 6.3, Advanced Development: All efforts directed toward the development of hardware for test. The primary goal is proof of the design concept rather than development of hardware for Service use. Two subcategories of advanced development are frequently used: (1) *6.3A, Non-System Specific Advanced Development:* Efforts that address techology options or uncertainty reduction for potential application to similar generic end products rather than to a specific, well-defined system. Includes development and technology demonstrations of components and subsystems. And (2) *6.3B, System Advanced Development:* Includes research and development efforts directed toward hardware for tests or experiments supporting the design of a specific system.

Category 6.4, Engineering Development: Those projects in full-scale engineering development for Service use, but which have not yet received production approval or had production funds included in the DOD budget submission. This area is characterized by major line item projects with control exercised at the individual project level.

Category 6.5, Management and Support: Support of installations and operations required for use in general research and development and not allocable to specific operational missions. Examples are major test ranges, broadly applicable test facilities, support of laboratories, and operation and maintenance of test aircraft and ships.

SUMMARY OF RESEARCH CATEGORY BUDGET REQUEST

[Thousands of dollars]

	Fiscal year—			
	1985	1986	1987	1988
6.1—Research	853,258	992,965	1,006,000	1,098,733
6.2—Exploratory development	2,273,768	2,510,646	2,737,175	2,941,466
6.3—Advanced development	6,750,403	9,920,959	12,013,348	14,001,156
6.4—Engineering development	10,471,347	10,552,547	11,931,368	12,128,684
6.5—Management and support	2,520,201	2,660,886	2,981,712	3,177,331
Research and development (FYDP program 6 totals)	22,868,977	26,638,003	30,669,603	33,347,370

Senator **Quayle**. Thank you very much.

Dr. Cyrus Knowles, vice president, R&D Associates.

STATEMENT OF DR. CYRUS P. KNOWLES, VICE PRESIDENT, R&D ASSOCIATES

Dr. **Knowles**. Thank you, Mr. Chairman.

I would like to remind you at the outset that this small panel is the only time you are going to hear about technology-base research. As our colleagues here have mentioned, this kind of research forms the front end of all major system procurements and thus has exceedingly high leverage.

Even though the amount of money involved in this kind of work is relatively small, and might go unnoticed in the larger scheme of things in the Congress, the implications of it are sufficiently profound that we urge you to consider this as a separate issue.

As people have noted, this kind of procurement is different from procurement of things. You cannot weigh or measure research. You cannot often define it in advance. It is a progressive process; one step leads to another, on occasion even to a Nobel Prize, sometimes to our surprise.

This kind of research comes from a variety of sources, Government laboratories, FCFR's, universities and, importantly, private industry.

I submit that private industry has been a major contributor to this kind of work over the years. In fact, in certain areas private industry represents perhaps the only resource available to the country.

Senator Warner's thought about nationalization of this work is, I think, right on the mark in that sense. If something is not changed, this kind of work will become nationalized.

I am not here to tell you specifically that industry is in trouble financially, at least not yet. There are perhaps some examples, but that is not the key point.

The key point is the ability of the Government to procure and manage first-class research. That is the important issue.

I have been involved in this kind of work for approximately 25 years, both inside and outside the Government, and I am seriously concerned about the erosion that I see taking place.

Let me give you some specific comments on CICA.

First, I believe the legislation and implementation discourages and perhaps eliminates unsolicited proposals for new and innovative ideas. You have heard that from the other speakers here and I wholeheartedly support that.

We are at a time when that kind of research is more important than ever. If we are going to maintain the technical edge that we have in the world, that kind of research forms the foundation.

There is, in passing, a problem with the CICA in that regard. The simple words "not otherwise available to the Government" which are included in the legislation can be interpreted in a variety of ways, one of which is forcing the Government to take ideas that are developed in private industry and put them out for competitive bid. You have already heard some examples of that.

Second, I believe the legislation and/or the implementation is decreasing the technical peer reviews that have historically taken place.

This kind of work is highly competitive, always has been highly competitive, but competitive on the basis of ideas, not on the basis of cost.

When we get into the situation where contractors feel threatened that sharing an idea can lead to someone else actually getting a contract, the technical interchange, that has historically taken place will vanish. We already see a tendency in that direction.

Third, interestingly enough, the CICA is tending to stifle competition and technical differences of opinion. The contracting procurement process, because of the legislation, is moving to longer-term and larger contracts, which makes good managerial sense.

Unfortunately, this freezes out smaller contractors and bidders who lose. So, the technical voice of opposition will be stifled.

Fourth, and I think quite importantly, there is a significant increase in both the financial and personnel cost to the Government. I have some examples of that.

The cost of proposal has increased from roughly $5,000 or $10,000 of overhead resource required to as much as $50,000 to $100,000 in order to win a competition. Given the fact that the cost is going up and more people are proposing on issues, the total cost to the Government is going up substantially. All of that, I remind you, is overhead cost.

In addition, technical personnel, both inside and outside the Government are experiencing a much larger fraction of their time processing paper.

I see the yellow light.

There is a significant increase of time associated with all this as well. I am not against competition, however, I am for competition of ideas.

Suggested course of action:

First. Accept the concept of competition of ideas to satisfy the goal of providing competition in contracting.

Second. As Dr. Rosenbaum points out, exempt 6.1, 6.2, and 6.3a programs.

Third. Through personnel review process, provide specific incentives for Government managers to procure innovative, effective, and timely research.

Fourth. Implement a streamlined procurement process that would provide for sole source contracting and would require that the majority of the research contracts be negotiated within 90 to 120 days.

I realize the changing legislation and/or implementation takes some time. Some of the problems, I recognize, may be in the implementation. Therefore, in the short term I urge the subcommittee to provide a written statement to DOD clearly indicating that it is the intent of the subcommittee that high quality tech base research should be encouraged and DOD should make every effort to expedite the process and procure innovative ideas.

I also urge the subcommittee and Congress as a whole to move quickly on this matter. Time is of the essence. If the procurement process breaks down, it may take a very long time to repair.

Thank you.

[The prepared statement of Dr. Knowles follows:]

PREPARED STATEMENT OF DR. CYRUS P. KNOWLES, VICE PRESIDENT, R&D ASSOCIATES

Mr. Chairman and members of the Subcommittee, I am Cyrus P. Knowles, Vice President and Manager of the Nuclear Weapons Effects Division of R&D Associates. I have been in the high technology research business for over 25 years, starting at Cornell University, and currently at RDA. I also recently spent four years within the government as an Assistant Deputy Director for Science and Technology, managing technology base programs, and two years in the Pentagon as an Assistant Deputy Under Secretary.

RDA is a company that was started in 1971 by the senior members of the RAND Corporation Physics Department and specializes in technology base research associated with nuclear weapons effects, tactical and strategic systems survivability and effectiveness, directed energy weapons and policy related issues. RDA is one of a number of companies that contribute to these highly innovative and often time urgent research areas. I am here today as a concerned scientist and as a concerned citizen to speak about issues that are vital to the United States and to a number of these companies—both large and small. Several corporate officers from these companies are here today.

I appreciate this opportunity to discuss our views of the implications of the Competition in Contracting Act (CICA) of 1984 on the performance of technology base research. The kind of research that I am talking about is quite different from types of procurement that you have been discussing during most of these hearings. It is important to distinguish between the procurement of things, that is, items that can be well specified in advance and can be checked against clear specifications upon delivery, and research that cannot be clearly and uniquely defined prior to the work. Indeed, if such precise definition were possible, it is likely that the research would not be needed because it has already been done. In the discussion that follows, then, I would ask that you consider the procurement of ideas as distinct from the procurement of weapon systems and piece parts.

Let me spend just a moment describing what this technology base research is all about. First, and perhaps most important, it has high leverage. This front end research defines the requirements for major strategic systems and provides the needed guidance for system design. If done well, it can produce systems like Trident II. If done poorly, it can result in things like the atomic airplane. While the amount of money is relatively small, this research impacts large system procurements in a fundamental way.

Second, this research is highly specialized. It requires unique talents that are not off-the-shelf commodities, but rather are the result of years of training of a relatively small number of highly specialized technical experts. In many areas, the technical community is quite small. Unlike part of the aerospace industry, a full page advertisement in the Los Angeles Times will not produce hundreds of applicants.

Third, this kind of research is already highly competitive—not in terms of cost, but rather in terms of ideas. The kind of competition that I believe you are looking for is already in existence, but is measured in terms of technical contribution.

The basic message that I am here to deliver today is not that the technology base industry is in trouble financially—although certainly there are instances where the legislation and its implementation have had serious impact—but rather that the Competition in Contracting Act and its implementation have diminished the capability of the United States to procure and manage the innovative technology base research needed to maintain the superiority of our strategic and tactical systems. I believe that truly first class research in these areas is needed now as never before and that it is essential that the Congress and the Administration do everything possible to encourage innovation and to procure timely and effective research.

This country's edge in technology has come from a number of centers of excellence—both large and small—in government laboratories, federally funded research centers, Universities and Colleges and, as importantly, in private industry. In certain areas, private industry has developed and maintained the bulk of the technical capability and in almost all cases, private industry had made major contributions toward the improvement of the technical understanding. The technical expertise now resident in a number of high technology private companies represents an important national resource but, unfortunately, one that is rather fragile. If not properly encouraged and managed, this capability could easily atrophy over time.

The problem, in a nutshell, is that ideas cannot be procured in the same way as hardware. Unfortunately this distinction is not sufficiently clear in the legislation, with the result that research procurement is generally being handled in the same way as the procurement of ships, planes and other military hardware. By making private industry researchers compete in this way, the government is pushing research towards its lowest common denominator. The emphasis is shifting away from technical excellence and proven capability towards minimum acceptable technical capability and minimum cost. Although the legislation has not been in force for very long, it is already becoming apparent that cost is a major factor in the award of research contracts. Under these circumstances, companies are motivated to propose low risk ideas with a minimum of uncertainties and to staff the work with more junior people in order to be competitive. While this approach can, in principle, save some small amount of money in the short term, it is likely to have a devastating effect on the quality of research—especially if this practice is continued. The problem was well stated by Dr. Robert Cooper in his recent statement before the Science Policy Task Force of the House Committee on Science and Technology:

"Recent changes to government procurement laws and the resulting Federal Acquisition Regulations (FAR) as well as the corresponding Defense Acquisition Regulations (DAR) have made contracting for Basic Research and Exploratory Development with both universities and private firms into a nightmare. This problem now ranks as the number one deterrent to efficient and timely development of new and innovative research efforts applied to Defense problems. It is a prime aggravation both to government program managers and to researchers and is creating consternation and ill will between them."

SOME SPECIFIC COMMENTS ON THE CICA

With this as background, let me now turn to some specific points:

1. The legislation and its implementation will significantly discourage—and perhaps ultimately eliminate—unsolicited proposals for new and innovative ideas that are developed within private industry.

Private industry has been a major source of new and innovative ideas that have provided significant contributions to the Department of Defense and the government in general. While many of these requirements have been forseen by the government and thus can be the subject of requests for proposals, many have been the result of individual creativity within the private sector. I believe that this creativity should be encouraged to the greatest extent possible. We must continue to tap this important resource if we are to maintain our technical edge.

One way to provide this encouragement is to reward the inventor of a new and innovative idea with a contract to develop the concept, at least through its early phases. Prior to the legislation, this was accomplished through the vehicle of a sole source contract. Assuming that the idea had technical merit and that it filled a legitimate need, the inventor generally has some reasonable assurance that he would be awarded a contract.

Unfortunately, the situation is rather different today. While provision is made in the legislation for sole source procurement, the words ". . . not otherwise available to the government" have restricted the implementation. If these are interpreted to mean: "Could the government obtain this idea from another company if the other company were given the original idea," then it is virtually impossible to have any sole source contracting. Ideas that are submitted as unsolicited, innovative proposals are often put out for competitive bid and, not infrequently, the contract is awarded to another company. Such a procedure is not likely to encourage innovation.

2. The legislation and its implementation is causing a decrease in the technical peer reviews and in the multi-discipline interactions that normally take place before a contract is let and after the work is in progress.

Prior to the Competition in Contracting Act, it was customary to have a number of technical review meetings to provide peer review. These meetings included open "no holds barred" discussions similar to the academic peer review that takes place in the university environment. The competition was intense, but it focused on the technical content and the innovation.

With the increased emphasis on cost competition, this technical interaction is tending to become inhibited. While we are all learning how to cope with the process, it seems clear that the technical review will suffer. Companies will become more and more hesitant to openly discuss their ideas for fear that the concepts will be used to unfair advantage by other contractors.

3. To some extent, the legislation and its implementation is tending to stifle, rather than enhance competition because smaller contractors can be locked out of large procurement actions.

Incongruous as it may seem, it is beginning to appear that the Competition in Contracting Act may reduce competition. As a result of the massive paperwork required to let competitive proposals, the government is moving to fewer, larger contracts that will run for a number of years. We already see evidence of contracts running for 3-5 years with renewal options for another 1-2 years. Under the CICA, this approach makes good managerial sense in an attempt to streamline the acquisition process, however it has the side effect of freezing out other contractors who would normally participate and thus reducing or perhaps eliminating any technical competition after the contract is let.

Because of the larger contract size, the smaller contractors with their limited staffs and limited overhead resources are forced into teaming arrangements with the larger companies and thus become subservient to them. Their independent technical contributions will be filtered through multiple layers of management before finding their way to the government.

4. The emphasis on competitive procurement will significantly increase both the financial and personnel cost to the government of doing research.

Because of the competition, the cost of preparing a proposal has increased significantly. While I have not developed a detailed data base from several companies, I believe that it is not uncommon for companies to spend $50,000 to $100,000 to prepare a proposal compared with about $10,000 for a sole source procurement prior to the CICA. Since several companies—perhaps as many as 5-7—are likely to bid on any given request for proposal (RFP), it is quite possible that between $250,000 and $700,000 of overhead would be spent in response to an RFP for, say, a $1-2 million contract. As a result, the overhead expense of each of the companies is likely to increase. Since this increase is a legitimate business expense, the costs will be passed on to the Federal Government.

Similarly, it appears that the number of man hours of government personnel required to process the procurement has increased dramatically. While precise numbers are not available, it is becoming clear that technical personnel within the government who are responsible for program definition and technical contract monitoring are spending a significantly larger fraction of their time on the paperwork associated with competitive contracting. It is estimated that the technical staff in the technology base research area are spending 40-50 percent of their time on contracting paperwork compared with about 15 percent a few years ago. This time is at the expense of their technical productivity.

A comparable situation exists within private industry. Senior technical personnel are spending more and more of their time "marketing" and proposal writing rather than doing technical work. This time is also at the expense of their technical productivity.

5. The legislation and its implementation has significantly increased the time required to process the procurement action, thus decreasing the responsiveness of the research and causing serious funding gaps for private companies.

Prior to the CICA, the average time required to process a procurement action was approximately 80-100 days. Today that time is estimated to have increased to approximately 200-285 days. The government agencies are now required to project technology base research programs 1½ to 2 years in advance and appear to have great difficulty in making substantive changes in less than 6-9 months. Given the dynamic nature of the research business, this situation seems intolerable. Research creates new ideas which lead to new research. The government should have the capability to aggressively pursue innovation in a timely way. While the legislation provides for a competitive advocate, it does not provide the balance of a "get-the-job-done" advocate.

Lest there be any confusion on the point, let me state categorically that I am not arguing against competition per se, Far from it. I believe that competition is essential in obtaining the best quality product for the government. What I am arguing is that in technology base research, the competition is a competition of ideas. Cost has little to do with the process, except that I believe that undue emphasis on minimum cost will insure minimum quality research. Remember that technology base research costs are primarily the cost of labor. Since all labor costs of a company are audited and approved by the government, the government does have control over the cost. In addition, the freedom of technical personnel to move from one company to another provides a leveling of salaries. The variation within the scientific industry is not likely to be large. Thus the emphasis should be on proven technical capability and innovation, not cost.

A SUGGESTED COURSE OF ACTION

Now let me turn to a discussion of a suggested course of action that could improve the situation. First and foremost, I believe that some relief from the current procurement practice is essential if the government intends to continue to acquire high quality, timely and innovative technology base research. There are a number of steps that could be taken to achieve that goal:

1. Accept the concept of "competition of ideas" as satisfying the goal of providing competition in contracting.

As noted previously, this competition is intense and focuses the attention of the researchers on the key issues, namely the technological issues, not the inconsequential differences in cost. Important standards for contract awards in the past have been past excellence in performance on similar contracts, the quality and experience of the contractors' technical personnel and his adherence to cost controls, observation and implementation of available economies and responsiveness to Government instructions. I believe that these standards should continue to be observed in the future as well.

2. Exempt all DOD 6.1, 6.2 and 6.3A funded programs from the provisions of the CICA.

These funding categories are specifically broken out to allow the monitoring of technology base research programs within the DOD. The aggregate of the three categories represents about 1.5 percent of the Defense budget. The intent would be to allow the government managers the flexibility to manage the high technology research in ways that would provide the needed output and timely response. With this exemption, such research would be treated in the same way that the CICA currently allows for educational or other not for profit institutions or federally funded research and development centers.

3. Through the personnel review process, provide specific incentives for the government managers to procure innovative, effective and timely research.

The emphasis should be on getting the job done and on providing a good, high quality product. The structure for this process is already in place through the various bonus and merit plans.

4. Implement a streamlined procurement process that would provide for sole source contracting and would require that the majority of research contracts be negotiated within 90-120 days.

Such an approach should lead to abbreviated proposals to minimize both the cost and the time of preparation and review.

I recognize that these steps may take some time to implement. I also recognize that some of the problem may lie in the implementation of the CICA rather than the legislation itself. In view of this, I urge the Subcommittee, as an interim measure, to provide a written statement to the Department of Defense clearly indicating that it is the intent of the subcommittee that high quality technology base research should be encouraged and that the DOD should make every effort, consistent with the legislation, to expedite the process and to procure innovative ideas. Such research is essential in maintaining the leading edge in defense. This statement could provide an excellent point of departure for a DOD wide review of the implementation procedures while the Congress considers the legislation.

I also urge the subcommittee, and the Congress as a whole, to move quickly on this matter. Time is of the essence. If the research procurement breaks down, it may take a very long time to repair.

Thank you.

Senator **Quayle**. Dr. Knowles, is DOD aware of the problems?

Dr. **Knowles**. At the working level, I believe they are. There are policy issues related to all of this that DOD is still sorting out.

Senator **Quayle**. What has been their response?

Dr. **Knowles**. The response at the working level is to try to find ways to live under the existing legislation and implementation, but, quite frankly, sir, I believe they are hamstrung at this point.

Senator **Quayle**. Hamstrung by what? The legislation?

Dr. **Knowles**. The part of the legislation having to do with two changes in legislation that I would urge.

One is the clarification of "not otherwise available to the Government," so that innovative ideas can be procured sole source.

And, second, is the basic exclusion of 6.1 to 6.3a that will treat private industry involved in technology-base research in the same way as the Government laboratories and FCRC's.

I think those two changes would go a long way toward moving back to the situation we had for quite a number of years that led to very excellent quality research.

Senator **Quayle**. It seems to me DOD would be as interested as you are in this. Yet I do not think that their testimony when they were up here came up with this thought. That is why I asked the question, is DOD aware of this?

Dr. **Knowles**. This county has a remarkable capability to postpone technology-base research. The defense budget is primarily spent on acquisition of things. Ninety-eight or so percent of the Defense budget is for things. So, the attention of the senior management in the Government, by necessity, is dedicated to those procurement actions.

Mr. **Rosenbaum**. I think much of the senior management in the Department of Defense is reeling under the kind of adverse publicity that they have gotten in the press on defense acquisition as well as that they have gotten in congressional response, both through legislation and through hearings. The tech base is a small problem in terms of total dollars and gets lost at high-level discussion.

The perception is very strong that Congress wants something different to happen in defense procurement and that something is cost competition for everything.

Dr. **Knowles**. The technology industry, I believe, is paying a terrible price for the $600 toilet seat.

Senator **Quayle**. There is a possibility that new ideas or breakthroughs or something like that will save millions, perhaps billions, of dollars.

Dr. **Knowles**. Absolutely.

Senator **Quayle**. Just one idea.

Mr. **Rosenbaum**. It takes 2½ years to get it under contract, though. First you have to divulge it, then you have to compete it.

Senator **Quayle**. How long did it used to take?

Dr. **Knowles**. Eighty to 100 days. Now it is taking 200 to 285 days to get it under contract.

Senator **Quayle**. That is because of CICA?

Dr. **Knowles**. Yes.

Mr. **Rosenbaum**. Specifically because of CICA.

Senator **Quayle**. I think your testimony is very interesting. Certainly we have not heard this before. I intend to ask DOD to substantiate and to respond to the revelations you have made here this morning. I am surprised that they have not.

Mr. **Rosenbaum**. There are various elements of DOD that are responding. The Naval Research Advisory Committee that I sit on is putting together a task force to look at this problem.

Senator **Quayle**. We did not have any testimony from the Naval Research Advisory Committee.

Does anybody have any examples of how the CICA legislation has actually stifled innovation, discouraged some ideas, personal examples you might give us?

Mr. **Hallamore**. We developed a product called break-free, which we developed for our commercial business. In reviewing some problems in the military, we saw the congressional inquiry on the M-16 rifle problem in Vietnam and also some other problems. We presented to the military a product that as a commercial product not only met what they called an impossible spec, but exceeded it in every case.

After much testing we finally became the sole source on that. Being sole source bothered a lot of people and, we believe, either tests or space were relaxed to achieve competition.

A little outfit called Shell Oil Co. is now a competitor of ours. Any company worth its salt supports its product in the field. In doing so, we recognized the severe problem of cleaning large caliber weapons. We came out with a system, a product line. We presented it in an unsolicited proposal.

Fortunately, we presented it before April 1 because it turns out April 1 seems to be a magic date on the lack of desire to accept unsolicited proposals. After much grinding of the teeth and with great effort, we now have this thing on contract. From that we have now gone on to recognize other areas of need in the military.

What we are getting now is a reluctance to accept an unsolicited proposal, specifically a new M-16 cleaning kit and a couple of other items.

We are also working with one of the most fantastic materials ever conceived and developed by Tupperware, which is a plastic that will not burn. Imagine in the interior of an aircraft a plastic that will not burn.

I am greatly concerned right now because of the problems that we have in acceptance of unsolicited proposals for new products because of this brownie point thing that the lower level contracting officers seem to have, if they get competition.

I am also concerned that we will be stubbing our toe going into some new development areas.

You asked for a specific and I think the specific that I will talk about ties into what the Army is now calling NDI, NonDevelopmental Items. I attended a classified meeting in Los Angeles where every general there said the magic term today is "NDI," NonDevelopmental Item. In effect, "You in industry create a product and present it to us that we can use, but you do it on your own money."

In operating that way, and we are doing that even though we are a small company, now comes the problem of how do you get on contract. We goofed on the testing for an M-16 cleaning kit. We corrected it on our own money. Now we are trying mightily to get on contract.

The NDI Program which the Army has adopted does not tie with the lack of desire to accept an unsolicited proposal. In fact, I asked a very embarrassing question in that meeting in Los Angeles, how do you, the Army, handle this thing? How do we get on contract if we in industry do go into an NDI Program?

The answer was: "We do not know. There will have to be some correction in the procurement process."

Senator **QUAYLE**. Gentlemen, unfortunately, another vote has come up. So, I think it is a good time to thank you for your very interesting testimony. I intend to follow up with the Department of Defense and see what their position is on this and hope they will take corrective action.

With that, the subcommittee is adjourned.

[Prepared statements submitted for the hearing record follow:]

Prepared Testimony of Peter H. Haas

The Competition in Contracting Act of 1984 (CICA) is generally a well conceived legislation to encourage competition in Government contracting and to assure that the Government obtains the best product at a minimum cost. All of us, as individuals, as taxpayers and as members of industrial organizations who contribute to the health and welfare of the country can readily support such objectives. We are, after all, used to their application in our every day life and see no reason why the Department of Defense should not require adherence to such basic premises in the conduct of its affairs toward assuring the nation's security. By far the vast majority of the funds authorized and appropriated by the Congress for defense are used to either pay personnel or procure military hardware. Legislation which provides for exacting standards toward competitive practices in the procurement of military systems and spare parts is a natural consequence of the American system used in both industry and other civil government practices. The CICA and its implementing regulation, the Federal Acquisition Regulations (FAR) additionally provide for the application of competitive practices in research and development. The large majority of R&D funds are expended for specific hardware development programs which are intended to lead toward subsequent production and procurement. All of these share one common feature: The item contracted for can be described sufficiently well before industrial bids and proposals are entertained so that a comparison with the delivered item can be made with reasonable exactitude in either performance or physically measurable quantity.

A much smaller portion of the military budget is dedicated toward research activities normally described under the program headings of 6.1, 6.2 and 6.3A. These programs normally constitute approximately 1-1.5% of the total DoD budget and even some of that relatively small amount is expended in the procurement of military hardware. The subject of this testimony is the yet smaller portion of the military research program (within 6.1, 6.2 and 6.3A categories) which does not contain the features described above, i.e., where the 'product' to be procured cannot a priori be described sufficiently well by either a measurable performance or by its physically measurable characteristics. Contract performance is here described in a 'Statement of Work' which contains a number of minimum goals the contractor is supposed to reach as part of his performance. Evaluation standards are furnished which further inform those who wish to propose on the contract precisely which features the Government wants emphasized and on what basis an award will be made. Relative priorities between the contractor's proposed approach toward reaching those goals, quality and quantity of manpower to be furnished, contractor's proposed pricing and other features are stated as well. Mostly, objective evaluations on how well the contractor has in fact performed on the Statement of Work are used in lieu of precise performance standards which could be measured after the fact on delivery. Since the vast majority of such contracts are of the "Cost plus Fee" variety, there is also the additional evaluation of how close he has come to a contractually agreed price.

It is clear that evaluation of competitively submitted proposals on this type of research contract is a more subjective than truly objective endeavor. Important standards for contract awards in the past have been past excel-lence in performance on similar contracts, the quality and experience of the contractors' technical personnel and his adherence to cost controls, observation and implementation of available economies and responsiveness to Government instructions. We believe that these standards should continue to be observed in the future as well, within the required language of the CICA. They have served both the Government and industry well in the past by allowing the Government to buy quality at a reasonable price and rewarding industry for superior performance through repeated contract awards where these were deserved.

It is equally important for the Government to be able to procure new ideas which lead to significant advances in technology and consequent advantages in military posture. At times such new ideas are the result of privately sponsored work in the industrial community--as well as in universities and frequently they result from research programs with relatively broad objectives sponsored by the Government with organizations possessing superior intellects. There are numerous 'centers of excellence' in various technical disciplines from which novel concepts have originated in the past. The CICA legislation has wisely provided at least in part for contracting for such efforts through several methods, one of which is the consideration of unsolicited research proposals. Such methods have been used with considerable success in the past, again to the advantage of both the Government and industry by giving the Government access to privately developed ideas without incurring fears of 'piracy' and by rewarding industry for investing in quality manpower and internal research.

The purpose of this testimony is to describe the shortcomings of the Competition in Contracting Act of 1984 and the consequent implementations in enabling the continuation of either of these features in contracting which have served the Department of Defense well in the past. We believe that much of the resultant problem lies in the interpretations and implementations of the Act, although some amendments may well be necessary to assure the continued health of Defense Research Programs, as well as the capability of many industrial organizations to effectively support them.

One can perhaps safely assume that a large number of research ideas originate as 'statements of requirements' within the Department of Defense. Most of these have their basic foundation within the needs of the fighting forces, to satisfy some requirement for a weapon or communication system. Others can be traced to questions dealing with the employment, deployment, effectiveness, survivability or lethality of some military concept, either already in existence or in an early conceptual stage. Finally, on a yet more abstract level exist complex studies to examine the political and military impact on the balance of forces caused by potential deficiencies in either our military systems or their deployments or their planned employments in case of conflict.

The trend of probability of origin of research ideas within the Government decreases from the first of those listed above to the last while the need for more unique and scarce professionalism increases sharply in that direction. The number of engineers and scientists who are able to translate a stated objective into an approach toward a solution with likely success in hardware development is by far greater than that of the highly trained mind with decades of experience and a wealth of background in discussions and debates with highly placed decision makers. Somewhere in the middle between these two more obvious extremes lies the area where the approach toward a solution is more likely to make the biggest difference in the quality of the product. Less experienced researchers are more likely to seek the easy and usually trivial path whereas those with substantially greater stature and background will choose the high ground offering far greater rewards. The Competition in Contracting Act (CICA) and its implementations have thus far proved to strongly favor the art of clever proposal writing and emphasis on relatively small monetary differences over demonstrated professionalism, past excellence in performance and uniqueness in approach.

We have stipulated earlier that at least some research ideas do not necessarily originate within the Government. One should now inquire how the Government can avail itself of the ideas which stem from innovation within the private sector. We are here speaking principally of approaches toward the solution of an unstated or unidentified 'requirement'; unstated because it had not been realized that new advances or novel approaches identified by some person or group in the private sector could provide a substantial improvement in either current capabilities or toward the solution of a problem previously thought beyond the state of the art. The situation here is quite analogous to that existent for a long time in our daily lives where a person's unique innovation becomes translated into a patent which gives him the right toward sole exploitation and reaping rewards from the public without the threat of competition which would encroach upon his invention. It would be equally foolhardy to state that even a majority of such ideas actually can originate within the Department of Defense than to state that the Government was the origin of most patents in the past. In fact, Defense Department personnel are sufficiently occupied with the pursuit of identified requirements and their implementation as to almost foreclose much thinking time toward innovation.

We can now turn toward an examination of how the Department of Defense presently deals with--and is permitted and encouraged to deal with--the two situations identified above, to wit:

- How to uniquely identify and select those substantially more qualified to perform on complex research and development problems

and

- How to take advantage of innovative thinking and creative ideas which can offer substantial rewards to the Department of Defense in the identification and implementation of new concepts.

One would like to believe that a competitive rating system should allow for the clear selection of the superior intellect, of the better performer, of the more knowledgeable organization staffed with greater competence and longer experience and at least in theory, capable of producing a better research proposal. In the first place, even if the above were true, the numerical qualitative rating system as actually practiced provides for only relatively small percentile differences between bidders. Organizations who are patently incapable of performing to a stated objective rarely even waste their time and scarce resources in a proposal; thus the number of bidders judged as incapable or unsatisfactory, below the line so to speak, is relatively small. Moreover, the technical evaluators frequently shrink from the resultant responsibility of explaining to such a bidder precisely why his product was found wanting. It is much easier to simply assign a relatively low, but still passing, numerical grade to such proposals. More importantly previous successes must be judged by those familiar with them; a simple citation of such high degrees of experience is available to nearly everybody through overstating the importance of relatively trivial pursuits and accomplishments and the difference is really only known to the personnel actually familiar with the real circumstances. Frequent changes of personnel due to rotation and transfers plus a common exclusion of 'familiar personnel' from evaluation boards to guard against 'cronyism,' disparage the use of excellence in past performance as a criterion. Judgements of greater competence and more diverse and deeper background become highly subjective when practiced by technical evaluation boards composed of relatively junior personnel of short term experience in highly specialized fields. An experienced proposal writer has relatively little trouble translating near irrelevant experience and shallow capabilities into an impressive resume'. The evaluator with long established experience in the field can tell the difference, by familiarity with the name alone, but as pointed out above, he is the exception. It is of course true that nearly every organization has some personnel at the management level who truly possess that background and that understanding. However, the vastly increased workload caused by insistence on a competitive spirit exhibited solely through the evaluation of written competitive proposals, makes it impossible for these management level personnel to actively participate in a major way in even a few, much less the greater majority of technical evaluations.

Under the extreme pressure of heavy workloads caused by the large number of increased competitive contract actions they simply have to depend on junior staff to perform the evaluation functions and can only be involved in abbreviated, final review actions.

A yet further detriment caused by the CICA has been the substantial increase in documentation and justification which have to be prepared in support of each contractual award by technical personnel, already heavily overloaded with the evaluation process. The inspections and audits conducted to assure the adequacy of this documentation have resulted in extreme overconservatism in the preparation of these papers in order to assure that the contracting process is not subject to yet further delays occasioned by protests or objections of auditors. The end result of all these added responsibilities is that technical personnel previously involved deeply with the technical supervision of the execution of the contracts spend nearly all of their available time in their preparation and justification. This imbalance would possibly be justifiable on relatively large contracts, especially those dealing with major hardware procurements, but is difficult to justify on the vast majority of relatively small contracts dealing with basic and supporting research and development. The added delays in the consummation of the contracts themselves is severely impacting needed flexibility in responding to urgent require-ments which could not have been forecast. The impact of these delays in contract negotiation on highly qualified scientific manpower is also responsible for disaffection of the most competent technical personnel from such programs and substantial increases in overhead costs.

The above unfortunate situation is, however, only the smaller part of the problem, since the technical evaluation, performed by a technical staff is only a part of the competitive awards process. Subsequent evaluations in the contractual process are fraught with immensely greater difficulties which apply not only to the first of the two situations, as stated above, but perhaps even more to the second; the one dealing with innovation.

The law itself as well as the FAR allow for ample consideration of proposals based on unique, innovative ideas, offered by a single organization, when not already subject to an identified Government requirement, and also not the subject of a current proposal request by the Government. One would believe that these conditions should allow for precisely the situation described earlier, analogous to the pursuit of a patent. It needs to be realized, however, that this provision is fairly well immersed within a long series of prohibitions, accompanied by citations of penalties for violation against awards to single sources without formal competition and requires advertising, higher level notifications and other strictures for a few, clearly spelled out exemptions. Any Agency head would be imprudent to say the least if he were not to be thoroughly and completely convinced that such proposals truly represent something unique and innovative. There are provisions in the law to help him in that regard. He is in fact required to initiate a market survey throughout the community of the Government to ascertain whether such an idea or approach has not already been considered elsewhere. This could in theory be helpful if the respondents could be relied on for true objectivity. In most actual instances there is likely to be at least one organization which is currently pursuing a 'somewhat similar,' but hardly analogous and frequently quite different research project which at its central theme is perhaps completely devoid of the very thing which makes the proposal in question unique and innovative. A reply which even hints that there are certain similarities can be sufficient to convince either the Head of the Agency or any of other individuals concerned with contractual awards that the proposal should now be rejected. Who are these other individuals who typically participate in these actions, whose concurrence needs to be obtained and what are their qualifications? At a minimum there is a General Counsel, i.e., an attorney, a Contract Specialist or Manager, perhaps some other administrative manager, plus a technical representative, or even several of these. The point is that in a military organization the majority of these are usually non technical personnel. To these the law has added a Competition Advocate and he more frequently than not is also non technical. The law in fact requires that this Competition Advocate be assisted by a staff to include "specialists in engineering, technical operations..." but this staff is rarely found in agencies dealing with the type of research and development discussed in this statement. The number of engineering specialists or personnel with substantive technical backgrounds interested in pursuing a career associated entirely with contractual issues is probably vanishingly small in any case and thus, the technical manager, who is also responsible for the conduct and successful contributions of the work, is the only person with a strong scientific/technical background capable of exercising solid judgment on the uniqueness and novelty of an unsolicited proposal. The details of the uniqueness and innovation in such proposals are nearly always quite complex. If they were easy and simple, someone else would have long ago discovered them. To expect a group of non technical personnel to appreciate them is undoubtedly asking too much and the evidence clearly shows that few, if any such, ideas survive this gamut. Several non technical voices, uncertain of the uniqueness of a proposal and strongly discouraged from any strictly non-competitive, single sourced, procurements will usually suffice to discourage any further encouragement toward innovation by the private sector through the technical staff. An easy way out of the dilemma turns out to be a decision that other organizations could also readily conduct this research, provide the same concept as has been proposed or that the uniqueness of the proposed approach has been insufficiently well demonstrated. The consequence of that decision is then a Government request for proposals to a wide spectrum of competitors, embodying some of the general principles of the original idea without violating any of its proprietory features. While this procedure may not actually discriminate against the originator of the novel concept, it results in two unfortunate conclusions. First of all, the Government does not promptly--and perhaps never--benefit from an original idea which could well have made a significant contribution to the technical balance. But equally important, it strongly discourages organizations in the private sector from spending any efforts toward innovation since it has become extremely difficult to evince active Government interest in these and moreover exposes such concepts to possible disclosure to competitors who had no need to invest in their discovery. It basically violates the very spirit of a well established custom in patents where the question is not who else could produce the same product but rather who first had the idea and pursued its implementation.

There is still further impediment toward selection of the superior performer or the innovator. In most agencies of the Department of Defense, as well as in its laboratories, there are technical managers who together with the head of the agency bear the central responsibility for the formulation and execution of the technical program and whose performance is evaluated on the basis of their success in contributions toward technical advances in defense matters. The responsibilities of the other personnel involved in contractual issues, while not at all non-commensurate with the above, are chiefly the enforcement of applicable regulations, to protect the head of the agency from violations and to support the technical staff. It is not difficult to understand why they are not easily persuaded by the lack of evidence of superior potential performance when presented with relatively small differences in numerical quality evaluations.

Errors in judgement in the technical evaluation or in subsequent contractual actions which result in awards that fall significantly below the Government's best interests in providing optimum products for the best price are near impossible to demonstrate after the fact in the type of research and development efforts discussed in this statement. After all, only one contract will have been let for each competition and the only requirement is for the performer to satisfy the minimum requirements of the contractual statement of work. Under the present implementations of the CICA, that contract is quite possibly the one submitted by the lesser qualified organization which, in order to become the winner, is perfectly willing to shave a few percentage points in price and which, with lesser competence and lower paid personnel, can readily persuade technical evaluators that their straightforward approach will, again at a minimum, satisfy the requirements of the contract. Since we are not dealing with a product which can either be strictly and exactly compared with pre-established standards of 'performance' or measured in some physical fashion for compliance with standards of accuracy, it will be difficult to show after the fact that a poorer product has been obtained. As long as the items listed in the statement of work have indeed been minimally satisfied there will be no comparison of relativity to someone else's potentially superior product since he never got the chance to perform. And the non-technical judge of the contract can not be proven to have been incorrect in his judgement.

What has been the result of the implementation of these ordinances? The 'Bid and Proposal' expenses of the private sector have clearly increased and that increase has largely been borne by the Government. If it can in fact be demonstrated that contractual costs as measured by labor and material dollars plus fee have decreased because of monetary competition, it could also be shown that such savings have been eroded by increased resultant overhead costs. The need of less successful bidding companies to acquire some of the more outstanding performers previously associated with other organizations can only be satisfied by offers of higher salaries; cost increases again borne by the Government with no commensurate improvement in either quality or competition. The long delays caused by technical and other contract evaluations have resulted in voids of contribution by some highly skilled, scarce personnel to the Government's needs. The very smallest companies, which also frequently have the lowest overhead rates and obviously very few contracts by comparison to the bigger ones will have great difficulty in surviving contract lapses, even if they were to eventually win their bids. They will be absorbed by larger corporations with no resultant gain to the Government. And perhaps worst of all, there has been and will continue to be, a drying up of new, innovative ideas being offered to the Department of Defense, since no organization can readily afford to spend its own resources toward the pursuit of such ideas only to have the Government offer something that will finally resemble the unique novel thought sufficiently for others to copy in a competitive venture.

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STATEMENT
on
RELIANCE ON THE PRIVATE SECTOR
for submission to the
SUBCOMMITTEE ON DEFENSE ACQUISITION POLICY
SENATE ARMED SERVICES COMMITTEE
for the
BUSINESS ALLIANCE ON GOVERNMENT COMPETITION
by
Frank Sellers

The Business Alliance on Government Competition ("the Alliance") is a coalition of 48 national trade and professional associations and other organizations — representing small and large businesses — who have a common interest in the federal government's long-standing policy of reliance on the private sector for needed goods and services. (A list of the members of the "Alliance" is attached.)

The federal government adopted a formal policy in 1955 that it would rely on the competitive private sector for the goods and services required for its own operation. Despite this policy, conservative estimates from the Office of Management and Budget (OMB) show that executive agencies spend more than $20 billion annually to provide commercially-available goods and services. Commercial activities in the Department of Defense (DOD) represent the major portion of that spending.

We strongly advocate more effective implementation of the 1955 policy of reliance on the private sector, as expressed in OMB Circular A-76. By more effective implementation, we mean more extensive application of the process as well as improvements in the process. Even at DOD, which has the most active implementation program, less than 10% of the activities which DOD has identified as available from the private sector have been subjected to cost comparisons since the cost comparison procedure was established.

Instead of increased reliance on the private sector, as expected under the Reagan Administration, we have witnessed an unprecedented expansion of federal government commercial activity. Moreover, at DOD alone, net civilian employment has increased by more than 68,000 in the past four years (civilian employment throughout the government has risen by more than 125,000). In the same period, the federal government has conducted cost comparisons on 35,000 positions, and conversions of federal government activities to the private sector have affected only 5,000 positions per year. At the current rate for performance of cost comparison studies, it will take more than 100 years to conduct one cost study of each commercial activity in the federal government.

At this stage, improvements must be made, or private contractors certainly will decide that it is more advantageous to pursue private market opportunities and avoid the problems inherent in contracting with the federal government.

In testimony on April 3, 1985, to the House Armed Services Committee, then Assistant Secretary of Defense, Lawrence J. Korb, left no doubt about the value of the OMB Circular A-76 program to DOD. "We view the A-76 program as competition, and very healthy competition at that. A-76 competitions save 29 percent of the original cost of doing business without harming, yet often enhancing, our ability to execute our mission. We have found that service often improves, while at the same time the cost of operations decreases."

The success noted by former Assistant Secretary Korb has come despite the flaws in the process. There are a number of structural factors which discriminate against the private sector as the A-76 process exists today. The following list includes some of the major problems:

Firm Contract versus Government Estimate - A contractor must submit a bid or proposal for a contract (usually firm fixed-price) which requires compliance with all terms and conditions and performance of all specified and implied tasks. When the same work is performed in-house, by government personnel, there are no such rigorous requirements and the government cost estimate is not legally binding. This is a severe disadvantage to industry but it varies so widely from case to case that it is difficult to quantify.

Overhead - A government contractor must allocate all overhead and indirect costs, on a consistent basis, between all contracts. This government requirement creates an unavoidable cost charged to each contract, but government cost estimates do not include any comparable recognition of indirect costs. Instead of a full allocation of government overhead, the estimate of government cost includes a marginal amount, if any. Conservatively, this injects a 20-30% disadvantage on the private sector.

Risk - The contract usually requires the contractor to accept risks for government property (even when the property is not under his control), for third-party liability, and for other contingencies which must be covered by insurance. The government is self-insured, and furthermore, the self-insurance factors are grossly understated compared to the rates that a contractor must pay. This produces a disadvantage on the private sector of 3-5%, and that disadvantage is growing steadily during the liability insurance crisis currently being experienced by the Defense industry and other industries.

Performance Penalties - Government contracts contain performance standards and penalty clauses which require a deduction from contract payments when these standards are not met. Since the standards frequently require perfect performance, the contractor must anticipate (and include in his bid) some penalty deduction for human error. There is no way to assess a financial penalty against a government work force that commits an error or delivers substandard performance. The average disadvantage here to the private sector is at least 2%.

Fringe Benefits - A contractor must include the full cost of Social Security, retirement, Workers' Compensation, and unemployment benefits in his costs. The fringe benefit cost factor for government employees has always been grossly understated, although this particular problem was partially corrected by the 1985 amendment of Circular A-76.

Contract Administration - Substantial costs are added to the contract price submitted to the government by the bidder for costs of monitoring contract performance. However, there is no comparable cost in the government estimate for "quality assurance." The cost disadvantage to the private sector is at least 3%.

Cost Differential - In any cost study of a current government commercial activity, a differential equal to 10% of the government personnel related cost is added to the cost of contract performance. Since most A-76 studies are for services, where personnel costs constitute more than 70% of the total cost, this produces a disadvantage of at least 7% to the private sector.

Despite these handicaps which, when added together, show the private sector to be at a disadvantage of at least 35% and often higher, we feel the private sector should still win the majority of cost comparisons because of the inherent economy which comes from competition. In fact, this belief was borne out in the first few years after the inception of the cost comparison study process in 1979, when approximately 80% of the cost studies resulted in conversion to contract.

The picture today is changed. The very resourceful bureaucracy has found numerous ways to construct solicitations so that they discourage bidding and increase the amount that contractors must bid. The unfair 35% handicap, when coupled with these tactics, is making it extremely difficult for the private sector to win any cost comparisons. As a result, some major companies are turning their backs on the A-76 program and the decreased competition will reduce the savings to the taxpayer.

These efforts by the bureaucracy constitute "bid-rigging" and are matters of "fraud, waste, and abuse" which this Committee has sought to control. These efforts inflate the amount of all bids to ensure that the activity either stays in-house or, when a contract is awarded, the cost is excessive. Some of these techniques (all of these have been used against the private sector) are:

1. Requiring a firm fixed-price contract when the work statement is written by the government agency in such an open-ended or generalized fashion that any company which bids must include large contingencies in its price. The result is less competition and greater cost whether converted to contract or continued in-house.

2. Using small business set-asides for the sole purpose of limiting the amount of competition. Once again, this results in greater cost and a better opportunity for the in-house estimate to win.
3. Requiring the prospective contractor to bid on the basis of furnishing necessary equipment or facilities, when such equipment and facilities already in use could be used by the contractor. These facilities and equipment are included in the government estimate at minimal cost, but new facilities will be a large cost in the contractor bid.
4. In negotiated procurements, rejecting lower-priced (than the in-house bid) proposals for being "outside the competitive range." This ensures that the bid which is accepted as feasible is higher than the government cost estimate.
5. Designating routine maintenance work as subject to the Davis-Bacon Act, instead of the Service Contract Act, so that the contractor is required to pay (and also cost in his bid) the higher labor rates applicable under the Davis-Bacon Act. In this scenario, federal agency work statements have made such things as changing light bulbs subject to the wage rates of the Davis-Bacon Act as prevailing in construction work.
6. Establishing minimum qualifications for contract personnel (licenses, training, etc.) which surpass the requirements for government employees performing the function.

At this point, one major step needed to address these problems is codification of the 1955 policy of federal government reliance on the private sector for needed goods and services. The General Accounting Office in 1978 recommended that the policy be enacted into law, and other reports and studies since then have endorsed that recommendation. Other organizations supporting codification --in addition to the "Alliance"-- include the Congressional Budget Office (CBO), the National Academy of Public Administration, the President's Private Sector Survey on Cost Control (the Grace Commission), and the Heritage Foundation.

Each of these organizations has recognized the need to exclude national security activities from mandatory reliance on the private sector, as provided in the current Circular A-76. The same exception has been included in all previously-proposed legislation, including Senator Warren Rudman's "Freedom From Government Competition Act," introduced in 1983 as S. 1746, and Representative Robert F. Smith's and Representative Charles W. Stenholm's "Contract Savings Act," introduced in 1985 as H.R. 3357.

The current concern for reaching deficit reduction targets would be well-served by codifying this policy and statutorily mandating implementation. The CBO and the OMB agree that annual budgetary savings of $1.1 billion could be realized from codification of the 1955 policy. Other estimates of cost savings are significantly higher, some as high as $20 billion per year. (This figure results from applying the average savings of 40% when federal government performance of commercial activities is contracted out to the estimated $50 billion being spent annually to produce goods and services by "sole-sourcing" to federal government employees.)

These savings would be repeated every year, even though contract costs escalate annually. (GAO studies have shown that cost increases in service contracts are comparable to cost increases that would occur in the case of in-house performance.)

Today's compelling need to reduce the federal budget and the budget deficit makes proliferation of government employment, without regard to relative cost, tantamount to fiscal irresponsibility. Clearly, the "make or buy" decisions of 1986 require a more rigid test of relative economy than in the past.

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COMMENTS ON LANGUAGE OF S-1783

1. General comments

It is our opinion that the concept of legislating work measurement is wrong. We believe that forcing of engineered standards where it can not be specifically proven that the effort will pay for itself will drive up the cost of weapons systems and will tend to stifle creativity in the defense industry.

While work standards have been used in the defense industry for a number of years, the creation of work standards by statute raises the spectre of an administrative morass and a paperwork burden of great proportion, especially considering the ever changing nature of such standards. Further, growth of robotics and other automated processes have changed the basic nature of various segments of manufacturing technology in recent years. It appears that there is no provision for the use of a cost/benefit analysis in its imposition nor for any determination of relief for type of contract or dollar value.

We therefore anticipate meaningful increases in costs of performance and adminstration of those contracts on which it is imposed, both within industry and within government.

2. The following specific changes to S-1783 are recommended:

a. Change the words "defense agency" in line 1 and 2 at the top of page 2 to read "contractor".

Reason: It has always been a matter of whether the contractor keeps the records not the agency. This appears to be a drafting error.

b. Change "180" days on line 10 page 2 to "360" days.

Reason: 180 days may not provide sufficient time for hearings on this very complex subject. The DoD authorization bill which this bill is amending was signed into law on November 8, 1985 (P.L. 99-145) which means the 180 days would end on May 8th, 1986. An alternative would be 270 days to allow time for the hearings and to formulate any changes or a decision to repeal the whole requirement.

c. Change the words "the date of enactment of such section" on lines 17 and 18 to read "the effective date under 2(a) above."

Reason: The existing language would make this requirement effective on November 8, 1985, the date the DoD authorization bill was signed when the objective of S-1783 is to delay the effective date to permit hearings on the subject.

d. Change the word "before" on line 20 of page 2 to "after".

Reason: This requirement should not be made applicable to existing contracts.

e. Delete the words "if such contracts have not been completed or otherwise terminated before such date" on lines 20 and 21 at the bottom of page 2.

Reason: Same as 4. Should not be made applicable to existing contracts.

f. Paragraphs c, d and e above could be eliminated if Sec. 2(b) (lines 13-21) on page 2 of the bill were deleted in its entirety. This whole sub-section deals with applicability to existing contracts which industry strongly objects to.

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COMMENTS ON AREAS NSIA BELIEVES HAVE GREAT ADVERSE IMPACT ON THE DEFENSE ACQUISITION PROCESS BY ADDING TO ITS COMPLEXITY AND COST

Enclosure
(Six(6) attachments)

COMMENTS ON AREAS NSIA BELIEVES HAVE GREAT ADVERSE IMPACT ON THE DEFENSE ACQUISITION PROCESS BY ADDING TO ITS COMPLEXITY AND COST

1. Audit (Defense Contract Audit Agency (DCAA)) Determination of Final Overhead Rates

a. Problem

There appears to be a common misconception that the long-standing practice of the Administrative Contracting Officer (ACO) negotiating final overhead rates at the larger contractor locations has resulted in: (i) negotiations in which the Government has allowed costs that should not have been recognized by the Government, and (ii) ACO negotiations considerably protracting the final settlement of overhead rates. These situations are not accurate portrayals of the facts.

The final settlement of overhead rates inevitably turns up costs which the auditor feels are unallowable whereas the contractor has determined that the subject costs are allowable. Seldom are these types of costs black or white. Various factors such as purpose, circumstances, timing, intent, volume, advance knowledge, legislative history, litigation history, etc. have to be closely examined. The fact that compromise and negotiation must logically take place is no reason to condemn the system. Some costs are determined to be totally unallowable, some are determined to be totally allowable, and other costs are negotiated with varying stipulations as to future allowability. To create a system where no negotiation or compromise exists is a naive and short-sighted position resulting in delay and considerable increase in disputes and litigation.

Historically, the auditor has challenged overhead costs as questionable or patently unallowable and then the ACO, a third party, after hearing the contractor's rationale, and after having reviewed the data with legal and Administrative Review Boards, has determined or negotiated a proper settlement. Even this reasonably straightforward system results in hundreds of court cases being filed each year by the contractor to properly adjudicate disputes.

DCAA management has publicly stated that they will not negotiate with the contractor. All DCAA determinations will thus be final -- and will undoubtedly result in a significant increase in litigation.

The misconception is that ACO responsibility for final determination of overhead rates has protracted settlement with the contractor and resulted in some contractor locations being 3-5 years behind on final settlement of rates. The DCAA, not the ACO, must bear the responsibility for delinquent settlement of rates. DCAA has historically placed a low priority on auditing final rates. At most contractor locations the ACO and the contractor have found it necessary to repeatedly follow up with DCAA and encourage them to place a higher priority on final audit of past years' overhead rates. Once a DCAA audit report is issued, final settlement has generally been very timely.

The present initiative of giving DCAA responsibility for final rate determination will undoubtedly result in additional delays in settlement of rates, increased litigation to settle DCAA's unilateral determinations, and no proven reduced costs to DoD.

b. Applicable Statute or Regulation

Deputy Secretary of Defense memorandum, Subject: Audit Determination of Indirect Cost Rates, dated 5 August 1985.

c. Action Needed

The Congress should recommend that the Secretary of Defense restore the ACO, at most major defense contractor locations, as the representative responsible for final determination of overhead rates.

The Congress should also recommend that the Secretary of Defense review DCAA's scheduled completion of past year audits and impose time constraints on DCAA completion of audits.

2. Lack of Regulatory Uniformity Among the Military Services

a. Problem

There have been several recent instances where the Navy has issued policies inconsistent with Office of the Secretary of Defense (OSD) guidance. These serve as fresh examples of a problem that is not new. The problem concerns the autonomy of the Services in issuing procurement policies without coordination among themselves or with OSD. The result of these actions is confusion, delay, inconsistency, and the furthering of Service parochial interests which may not be in the best interest of the Department of Defense.

The below referenced Navy policies were issued without benefit of adequate research or public comments. The August 7, 1985 memorandum issued by Assistant Secretary Pyatt, was withdrawn at the direction of the Deputy Secretary of Defense on October 30, 1985 because it conflicted with the requirements of the Federal Acquisition Regulation. SECNAV Instruction 4210.6 establishes policies requiring contractors to invest their own funds in production tooling and test equipment and mandates the use of fixed-price type contracts for full scale engineering development. Several assumptions contained in the instruction that serve as the basis for the policies are incorrect. This would not have occurred if the instruction had been subject to public comments. These policies are radical departures from current practices and may violate the law. Attached are three papers (Attachments 1,2,3) which outline the problems with SECNAVINST 4210.6.

b. Applicable Statute or Regulation

SECNAVINST 4210.6, Subject: Acquisition Policy, dated 20 November 1985; ASN(A&L) memorandum, Subject: Contract Cost Reasonableness Criteria, dated 7 August 1985.

c. Action Needed

1. The Congress should recommend that SECNAVINST 4210.6 be withdrawn. Future Service issuances should be coordinated within DoD.

2. The Congress should recommend that the Services be required to publish for public comment, prior to implementation, any policies that affect DOD acquisition.

3. The Congress should also recommend that 10 USC 2303a, (Publication of Proposed Regulations), which requires public comment on proposed policies and regulations, be enforced and that the waiver authority subsection (d) be tightened.

3. Legislated Work Measurement Standards

a. Problem

As stated in our letter of 4 December 1985 to the Subcommittee, NSIA supports the purpose of Senator Levin's introduction of S.1783, which seeks to delay implementation of the Boxer/Grassley amendment to the FY '86 Authorization Act to permit hearings by the Senate on these experimental provisions. Defense specifications and small, batch-type production runs common to Defense manufacturing make the process of developing commercial style work standards a complicated process of dubious practical value, at best.

It is our opinion that the concept of legislating work measurement is wrong. We believe that forcing of engineered standards where it cannot be specifically proven that the effort will pay for itself will drive up the cost of weapons systems and will tend to stifle creativity in the defense industry.

While work standards have been used in the defense industry for a number of years, the creation of work standards by statute raises the spectre of an administrative morass and a paperwork burden of great proportion, especially considering the ever changing nature of such standards. Further, growth of robotics and other automated processes have changed the basic nature of various segments of manufacturing technology in recent years. It appears that there is no provision for the use of cost/benefit analysis in its imposition nor for any determination of relief for type of contract or dollar value.

We therefore anticipate meaningful increases in costs of performance and administration of those contracts on which it is imposed, both within industry and within government.

b. Applicable Statute or Regulation

Section 2406(c) Title The U.S.C. as added by Section 917 of the Department of Defense Authorization Act, 1986.

c. Action Needed

Repeal of above legislation in recognition of the inherent differences in the defense manufacturing environment versus its commercial industry counterparts.

4. P.L. 91-441, Section 203 (Independent Research and Development/Bid & Proposal)

a. Problem

The DOD practice of agreeing to dollar limitations on IR&D/B&P is in contravention of P.L. 91-441 and is of extremely questionable legal validity.

The DOD practice of negotiating ceilings on a percentage limited increase of the preceding year's ceiling ignores the provisions of P.L. 91-441. Ceilings should be negotiated on each year's planned expenditures in accordance with P.L. 91-441.

Industry's problem is not with P.L. 91-441--we can live with the law if DOD will implement it properly. The problem is with the practice of DOD to completely ignore the law and its practice to resort to "forced cost-sharing" in establishment of ceilings. Industry's continued dialogue with DOD over the past decade has resulted in one minor success - the removal of ceiling limitations on the pricing of FMS sales. That success was achieved only after a long harangue that conclusively showed the legal fallacy of the original premise underlying the ceiling imposition on FMS Sales.

Each year,DOD is realizing the full benefit of hundreds of millions of dollars of technological effort without paying its fair, allocable share for such effort.

Unless some concerted action is taken by the Congress, the problem will continue year after year, and probably get worse due to increased bidding costs as a result of the Competition in Contracting Act.

Although costs for IR&D/B&P effort have risen dramatically in the past decade, actual hours expended for IR&D have remained reasonably constant.

In addition, there is a great loss of work time by engineers and scientists in brochure preparation and review that could be better spent on scientific endeavor by contractor personnel. This is also true of on-site technical reviews. A third cost is the application of overhead to IR&D/B&P which doubles IR&D/B&P cost statistics. The process has become a formula application which gives little or no recognition to the differences in business requirements or technical excellence of each contractor.

See Attachment 4

b. Applicable Statute or Regulation

P.L. 91-441 Section 203.

c. Action Needed

The Congress should recommend that DOD treat IR&D/B&P as any other overhead and apply the test of reasonableness so DOD pays its fair share of IR&D/B&P costs, and unproductive time by scientists and engineers is minimized.

5. Selected Laws and Regulations Aimed at Achieving Socio-Economic Objectives

a. Problem

It has long been recognized that the sheer magnitude of government procurement funds creates a tremendous leverage and opportunity for implementation of certain national policies not directly related to the subject of the procurement process itself. Thus, government suppliers are contractually subjected to selected public policy standards which are more stringent than those imposed upon the commercial sector. These relate, for example, to employment practices, working conditions, wages, environmental standards, preference for domestic goods, and rehabilitation of the handicapped.

The principal problem raised by use of the government contract as an instrument of national social and economic policy is one of administrative delay and increased cost. The overlaying of the requirements upon the process of purchasing government needs has the cumulative effect of further complicating an already extremely complex administrative task. While such delay and cost have not been quantified, it is an accepted fact that they are substantial.

b. Applicable Statute or Regulation *

The 1972 Report of the Commission on Government Procurement analyzed this subject. Enclosed as attachment 5 is the list of "social and economic programs" based on statutory and regulatory requirements which its recommendations dealt with. Since the Commission's table was prepared, regulatory requirements have generally been translated into current regulations.

c. Action Needed

The Commission made a number of sound recommendations addressing this problem. The Congress should reexamine these recommendations and assure that they are acted upon where appropriate. They include:

(i) The establishment of a comprehensive program for legislative and executive branch reexamination of the full range of social and economic problems applied to the procurement process and the adminstrative practices followed in their application.

(ii) Raising the dollar thresholds at which social and economic programs are applied to the procurement process.

(iii) Consideration of means to make the costs of implementing social and economic goals through the procurement process more visible, and

(iv) Revision of debarment policies to provide for uniform treatment of the various social and economic requirements and to establish a broader range of sanctions for such violations.

*See Table 1, Social and Economic Problems. Report of the Commission on Government Procurement, Vol. 1, Dec. 1972, pg. 114 et. seq.

6. P.L. 87-653 Truth in Negotiations Act (Criminalization)

a. Problem

The Truth in Negotiations Act was never intended to serve as a basis for criminal action. However, the Government is attempting to cast cases involving inadvertent defective pricing in terms of criminal tones. There is even proposed legislation (S.940) which would negate all of the legitimate defenses to defective pricing cases which have been recognized by the Boards of Contract Appeals.

Most defective pricing situations do not stem from criminal conduct. They are usually based on a lack of knowledge of the requirement for certified cost or pricing data, inadequate estimating procedures, inadequate management review and control of the estimating process, or inadvertent errors or oversight by the contractor's staff responsible for pricing and negotiating Government contracts and subcontracts.

Although the Act itself does not contribute to criminalization of the procurement process, the adequate civil remedy provided for under the Act is being distorted because of the use in typical defective pricing situations of the criminal statutes by the Government such as the False Statements Act, 18 U.S.C. 1001(f).

b. Applicable Statute or Regulation

The Truth in Negotiations Act P.L. 87-653 (10 U.S.C. 2306(f))

c. Action Needed

A statutory amendment (to the Truth in Negotiations Act, or otherwise) is needed that would include a mechanism for tightening the standards for securing criminal conviction based on alleged violations of the Truth in Negotiations Act.

7. P.L. 87-653 Truth in Negotiations Act (Dollar Threshold)

a. Problem

The requirement to provide data on such relatively low priced negotiated contracts ($100,000) increases the time and cost of preparing proposals, increases the number of audits performed both before award and after award, and delays negotiation and execution of contracts, thereby increasing the leadtimes between requirement identification and contracting. It also increases subcontracting administration requirements, delaying subcontract awards and overall contract performance. We are convinced that costs saved, if any, in the contract price are not sufficient to justify the time and expense involved in the administration of this procedure. The $100,000 threshold is simply too low in the world of today. For example, even if you presume a 10% saving on a $100,000 price (i.e., $10,000) it can easily cost that much or more for audit, information search, retrieval, copying, transmission, evaluation, and associated delays.

b. Applicable Statute or Regulation

The Competition in Contracting Act, P.L. 98-369, made the requirements of the Truth in Negotiations Act applicable to civilian agencies by amending the Federal Property and Administrative Services Act (41 U.S.C. 254), and lowered the threshold for requirements to provide and certify costs and pricing data from $500,000 to $100,000.

c. Action Needed

Raise the threshold to at least $1,000,000.

8. Statutes and Regulations Contributing to Criminalization of the Procurement Process

a. Problem #1

The 1986 DoD Authorization Act imposes a penalty of $10,000 for each contractor's proposal for settlement of indirect costs under all contracts over $100,000 ("other than a fixed-price contract without cost incentives") that includes items of unallowable cost plus the further penalty of double the amount of such cost if that item of cost has been previously disallowed. Criminal exposure is further increased by the requirement (Section 911) that the contractor certify that all such costs "are allowable" to the best of his knowledge and belief. The reality is that the allowability of cost cannot be determined with the exactitude that this new law presumes. The widespread "gray areas" and overlaps between allowable and unallowable contractor costs are inherent in the process and will continue to plague the contracting parties when acting in good faith in this important matter of contract administration. Obviously, matters of this kind are best left to contract negotiation and to prosecution only when fraud is clearly evidenced.

b. Applicable Statutue or Regulation

1986 DoD Authorization Act: Unallowable Costs

c. Action Needed

This provision of the 1986 DoD Authorization Act should be repealed.

d. Problem #2

With respect to false claims, the Act enlarges the penalties of the Criminal False Claims Act from $10,000 to $1,000,000, and those of the Civil False Claims Act from double to treble the Government's damage. But since these changes would only apply to false claims in relation to DoD contracts, as distinguished from false claims on other Government contracts and other federal programs, the unequal application and unequal protection of this law, as so enforced, raises fundamental questions of constitutional violation. If the penalties for violations of these laws are to be increased, Congress should do that on a Government-wide basis or not at all.

e. Applicable Statute or Regulation

1986 DoD Authorization Act, Section 931, Amendment to Criminal False Claims Act.

f. Action Needed

This provision of the 1986 DoD Authorizaiton Act should be repealed.

g. Problem #3

This provision of the DoD Authorization Act is most symptomatic of the criminalization of the procurement process. It grants documentary subpoena power to the Director of the Defense Contract Audit Agency in relation to DoD contractor records, to which access is otherwise granted by 10 U.S.C. Subsection 2306(f) and 2313. This power, paralleling that of the DoD Inspector General, will surely be exercised unsparingly to hunt for fraud in the costing of DoD contracts subject to the cost and pricing data requirements of 10 U.S.C. Subsection 2306(f). The disappearance of the long-standing separation of contract administration from criminal investigation will likely accelerate an addition to the erosion of mutual cooperation between contractor and contracting officers. DCAA auditors (like contracting officers and other procurement personnel) should not be allowed to become criminal investigators reporting to Department of Justice prosecutors.

h. Applicable Statute or Regulation

1986 DoD Authorization Act--DCAA Subpoena Power.

i. Action Needed

This provision of the DoD Authorization Act should be repealed.

j. Problem #4

The same tendency to criminalization of contract administration is evident in Section 917 of the 1986 DoD Authorization Act. It will require, for contracts over $100,000 made with certified cost and pricing data, contractors to record, and for the first time provide to the Government on fixed-price type contracts, the incurred costs of contract performance by the same categories as they were proposed and negotiated in arriving at the contract price. This disclosure of incurred costs will greatly facilitate the prosecution of contractors for submitting defective cost or pricing data. Thus, the tendency of contractor audits to become fraud hunts will quicken even more than its current accelerated pace. For that reason alone, these disclosures should not be required in the normal course of contract administration.

k. Applicable Statute or Regulation

1986 DoD Authorization Act, Section 917--Additional Disclosures of Data

l. Action Needed

This provision of the 1986 DoD Authorization Act should be repealed.

m. Problem #5

The Department of Justice has referred to Congress a package of eight bills entitled, "The Anti-fraud Enforcement Initiative," which if passed in whole or in part, are destined to have traumatic effects on the procurement process. This is part of the Government's continuing criminalization of the procurement process and is supplanting the traditional buyer/seller relationship with criminal investigators armed with immense, unchecked powers. These powers,, if employed as expected, will have serious impact upon the Fifth Amendment self-incrimination rights of contractor employees as well as serious implications for contractor Fourth Amendment rights to be free from unreasonable search and seizure. In addition, the proposed legislation could violate contractors' Fifth Amendment rights to be investigated and indicted by Grand Jury. This package of proposed legislation constitutes the most obvious example of the insidious trend toward the blurring of any distinction between criminal and civil investigation of Government contractors and any distinction between criminal/civil investigation and certain functions of contract administration.

Because the bills would undermine procedural safeguards guaranteed by the United States Constitution, they could only serve to further disrupt the Government's procurement system.

n. Applicable Statute or Regulation

Proposed Legislation

o. Action Needed

The Congress should review and eliminate those aspects of the five bills that would undermine procedural safeguards guaranteed by the United States Constitution to those who find themselves under criminal investigation.

p. Problem

The proliferation of certificates required of contractors in the procurement process is part of the Government's emphasis on criminal law and criminal investigation as a tool for ensuring contractor compliance. These certificates set the stage for charges by the Government that contractors have violated a number of laws, principally the False Statements Act (18 U.S.C. 1001) and the False Claims Act (18 U.S.C. 287). The certificates identified above and their use as a tool for prosecution of contractors is creating an intensely adversary atmosphere between the Government and its contractors to the detriment of the acquisition process. Contractors feel that the Government is attempting to entrap them into making unwittingly false or inaccurate certifications. In many instances, contractors are having difficulty finding anyone in their organizations to sign the certificates even though none of the eligible employees believes that the certifications are inaccurate or false.

q. Applicable Statute or Regulation

Federal Acquisition Regulations 52.203-02, Certificate of Independent Price Determination; 52.222-21, Certification of Nonsegregated Facilities; 52.223-01, Clean Air and Water Certification; 52.223-04, Recovered Material Certification; 52.225-01, Buy American Certificate; 52.225-08, Balance of Payments Program Certificate; 52.230-01, Cost Accounting Standards Notices and

Certification (National Defense); 52.230-02, Cost Accounting Standards Notices and Certification (Nondefense); 52.246-15, Certificate of Conformance, et al.

r. Action Needed

The Congress should recommend that the Secretary of efense reeview all certificates should be reviewed by the Department of Defense to ensure that only those which serve a clearly articulable Government need in the acquisition process be retained. Those certificates retained should include language which makes clear that the individual signing the certificate is certifying to the best of his or her knowledge and in good faith.

9. Application of Excessive and Overly Complex Military Specifications

a. Problem

There are over 40,000 Military Standards and Specifications applicable to DoD contracts. Many are technical in nature. Many others contain specific ("how to") procedures as opposed to general or objective criteria.

The prevailing practice of the DoD is to incorporate technical specifications and standards, and by reference in those documents to other specifications and standards, in contracts without clarification or limitation. If not current, and if not tailored to the relevant conditions of today's industries, these specifications and standards can prevent contractors from using their current procedures, require use of management techniques which are obsolete, unnecessary, or inappropriate, and to pursue costly and disruptive contract deviation procedures to avoid obvious waste.

Many technical specifications have become excessive and should be eliminated.

Concerning "how to" specifications and standards, their increased use by the DoD acts to constrain and reduce substantially the ability of the contractor to develop and employ advanced and cost-effective solutions to the functional and operational performance reequirements of weapon systems.

(A more detailed discussion of these problems is at attachment 6, which was prepared by a member company for the Packard Commission.)

b. Applicable Statute or Regulation

Deputy Secretary of Defense memorandum, Subject: Acquisition Streamlining, dated 3 June 1985.

c. Action Needed

The Congress should recommend that the policies contained in Deputy Secretary of Defense memorandum dated June 3, 1985, be aggressively and broadly implemented within the Department of Defense.

10. Laws and Regulations Requiring Excessive Reporting

a. Problem

The Department of Defense, the acquisition process, and contractors at all levels are burdened by excessive reporting requirements. Chapter 9 of S-Prt 99-86, Defense Organization: The Need for Change, Staff Report to the Committee On Armed Services United States Senate, reports an increase of more than 1000% in the number of reports required by Congress of the Defense Department between 1970 and 1985. (p. 592)

Reports required of contractors have also increased though no statistics are available.

Reports required of contracting officers, auditors, program managers and others have also increased.

While some reports may be necessary and valuable, the present requirements are excessive and contribute to the costly stretchout of the acquisition cycle.

b. Applicable Statute or Regulation

The precise identities of the statutes and regulations which give rise to the problems discussed herein are too widespread to permit ease of identification. One of the major statutes however is the annual Defense Authorization Act.

c. Action Needed

(i) Move to two year authorizations and appropriations for DOD. This should automatically reduce reporting requirements.

(ii) Eliminate as many reports as possible from future authorization acts.

(iii) Repeal P.L. 91-441. (Refer to comments on P.L. 91-441, Section 203 Independent Research and Development/Bid & Proposal).

(iv) The Congress recommend to the Secretary of Defense that he reduce reporting requirements to the maximum extent.

(v) The Congress recommend to the Office of Management and Budget (OMB) that the OMB more effectively implement the Paperwork Reduction Act.

11. Regulations Impacting on Technical Data Rights and Reporting Requirements

a. Problem

The Congress specified in P.L. 98-577 that the government should obtain rights to data. The language suggested limiting a contractor's rights in data to a period of seven years as a negotiation objective. The language is sufficiently stringent in that it essentially mandates using seven years as an unnegotiable maximum and suggesting that a lesser time is desirable. Recent experience seems to indicate a general tendency of DoD to obtain data in such short time frames even though the items being considered for procurement may warrant longer time periods. We believe that over-emphasis on abrogation of contractor rights in data may stifle innovation in the government marketplace.

Section 1213 of the FY 1985 DoD Authorization Act established the surrender of technical data as an element of competition. It enables DoD to demand the surrender of technical data, whether it is needed or not, as part of the price offered.

This approach burdens rather than aids competition. By providing competition through surrender of data rights a company's position on pricing is seriously weakened. Its ability to include the price of development in its production items, as it must in any government or defense contract, is elimInted. Competition is healthy for the procurement system only if the competitors are permitted to recover their investments and strengthen their ability to continue developing technology which gives them and their systems a competitive advantage.

The Government for years has required that a contractor provide technical data and drawings relating to hardware being delivered under contract. Such data often includes trade secrets or other proprietary material which the originating contractor is unwilling to disclose. Accordingly, a contractor is permitted to limit the Government's "right to use" if the technical data is unpublished and pertains to an item, component or process developed at private expense.

The Defense Procurement Act and the Small Business and Federal Procurement Competition Enhancement Act of '84 mandated new technical data regulations. The resultant regulations were published in the fall of 1985 and were subsequently withdrawn primarily due to objections raised by the industry concerning the over-implementation of the statute. A more simplified version was then published as an interim rule pending final analysis and publication of a final rule expected sometime in early 1986:

o The rule requires that a contractor provide unlimited rights in any technical data or computer software used by the contractor or any subcontractor or supplier at any stage of manufacture or development of the item being delivered under the contract.

o The rule states that a contractor's willingness to provide such data and rights may be evaluated as part of a source selection, whereas the Defense Authorization Act of '84 states the contractor will not be required to provide technical data for commercial products or processes as a condition for obtaining a contract.

o The rule permits the Government to order data at any level of detail wihin a product configuration that has been previously produced even though not currently under a contract.

o The rule ignores an imperative of the "Defense Reform Act of '84" wherein it is stated that regulations implementing the Act shall take into consideration how the technical data development was funded.

b. Applicable Statute or Regulation

P.L. 98-577 Section 1213, FY 85 DoD Authorization Act

c. Action Needed

With reference to P.L. 98-577, language specifying a seven-year time frame for acquisition of rights in data should be eliminated.

(With reference to Section 1213 of the FY 85 Authorization Act, inasmuch as the final regulations have been withdrawn it is too early for industry to determine whether there is or will be a regulatory "over-reach"of the statutes. However, if the regulatory guidance issued by the Air Force and Navy since the legislation was enacted is indicative of what OSD eventually issues, the industry will once again face a serious statutory overreach on the part of DoD.)

12. Spare Parts Breakout Regulations

a. Problem

The Small Business and Federal Procurement Competition Enhancement Act (P.L. 98-577), signed into law in October of 1984, calls for the assignment of a Small Business Administration breakout procurement center representative at every procurement center spending $150 million or more on spare parts, and to other centers as selected by the SBA. To assist this representative, SBA must assign at least two technical advisors.

The responsibility of these SBA officials is to exert every effort to increase the breakout of items for procurement.

The breakout concept is not new, having been first defined in the DoD High Dollar Spare Parts Breakout Program of March, 1969. The Congress was obviously displeased with the implementation of that program.

The Office of Federal Procurement Policy, at the direction of the Congress, made a study of DoD spare parts procurement practices in the first half of 1984. Their report, dated June, 1984, noted the spares reform programs of the military Services and the Defense Logistics Agency. Breakout was one of the areas listed as being "structured for significant improvements."

The OFPP Report made eight major conclusions, the fourth being: "In the near term, the most difficult aspect of the program is the implementation of a cost effective breakout program." The Report also stated that the breakout program recognizes that not all spare parts should be subjected to competition. To quote the Report: "Certain parts are so critical that a failure could have catastrophic results."

The OFPP made a number of major recommendations, the first of which stated that the Congress should continue oversight of the reforms initiated by DoD, "but hold off on legislative action until these reforms have had a chance to produce results. The reform programs will take several years and any additional legislation at this time could be counterproductive."

The Congress chose to ignore that recommendation, and to pass substantial legislation dealing with spare parts, including breakout, as noted above.

As an early reaction to the spares "horror stories," defense industry offered thousands of parts to the DoD as candidates for procurement from the original source; in effect, a volunteer breakout program. Meanwhile the DoD proceeded to hire thousands of new employees to work on spare parts problems at the buying centers. This points up the labor-intensive nature of spare parts procurement management, especially the breakout function. Thus, the management of many thousands of broken-out parts has been transferred from contractors to the DoD. This action has not been without turbulence to the procurement system and is typical of the over-reaction which so often accompanies a change in government policy made in the glare of publicity and under the critical gaze of the Congress.

For instance, the press contained stories in early 1985 dealing with the cannibalization of reserve engines for parts for its two principal fighter aircraft. Internal Air Force documents blamed this problem on putting spare parts up for competitive bidding rather than relying on a relatively small group of suppliers. "The growing pains of this breakout are evidenced by many of the new vendors failing to perform at all or producing inferior parts," the Air Force document states.

In addition, procurement leadtimes for many spare parts have lengthened. The Air Force has stated publicly that it took 58 days in 1983 to buy jet engine spare parts, and today it takes 159 days.

In summary, the NSIA appreciates the basic philosophy of breakout when such action will result in effective support of defense equipment and in lower prices for quality parts. Indeed, NSIA has supported the breakout actions of DoD in the past. We do not, however, support the acceptance of parts for management by the DoD when that agency's resources are not geared up to accept them, and when the possible impact on readiness of such transfer of management has not been carefully evaluated in advance. Precipitous breakout actions increase the cost of spare parts procurement, and endanger the readiness of the armed forces.

b. Applicable Statute or Regulation

(1) DoD High Dollar Spare Parts Breakout Program, March 1969.

(2) The Small Business & Federal Procurement Competition Enchancement Act (P.L. 98-577), October, 1984.

c. Action Needed

The Congress should recommend that the Secretary of Defense direct the Military Services and the Defense Logistics Agency not to request, or accept, the transfer of management of spare parts before careful analysis of the complexity of such management is made. The Services and DLA should also be prepared to demonstrate that they possess the technical expertise necessary to meet the anticipated needs of the active forces where such parts are involved.

13. Regulations Establishing Various "Advocates"

a. Problem

For many years one of the principal strengths of the DoD procurement system was the overriding authority and responsibility of the contracting officer in dealing with all contract matters. This authority and responsibility has become eroded in recent years by the designation of numerous advocates to question the contracting officers' decisions. This has had a deleterious effect on the the procurement process and the relationship of the DoD and its contractors.

Much of the basis for the recent efforts to reduce the role of the contracting officer rests on the concept that "the procurement system needs fixing;" a concept proclaimed by some members of the Congress, and repeated often in the media.

In regards to "advocates," the earliest was the small and disadvantaged business representative, a position created many years ago. That advocate's job is to represent the interests of his constituency, the small and disadvantaged businessman, at the buying centers of the government. This includes a close surveillance of the contracts approved by or under the consideration of, the contracting officer.

More and more power has been given to this advocate, and a significant body of legislation now exists as a basis for his challenging of the actions of the contracting officer.

Over the past 30 years the use of the procurement system to further the best interests of the small and disadvantaged businessman has become an accepted fact. The creation of small business committees in the Congress, serviced by large staffs, assures that this will remain an accepted fact. However, the cost-versus-benefits of this effort, along with the many other socio-economic programs carried by the procurement system, are highly questionable. As the Commission on Government Procurement noted in its 1972 Report, "More deliberate attention and analysis should be given to the nonprocurement obligations placed on the procurement process and to the consequences that are adverse to efficient and economic performance."

The Breakout Procurement Center Representative (BPCR) was created by legislation in 1984 to assure that the actions of the contracting officer provided a breakout of parts for competition, and for additional sources, to the greatest possible degree. This places the breakout advocate in a position to question the procurement decisions of the contracting officer.

The most publicized, and undoubtedly the most powerful, of those positions created to monitor the perfomance of contracting officers is that of Competition Advocate. In fact, some of the Services established these jobs before the Competition in Contracting Act of 1984 was passed. These advocates are at either senior civilian or general/flag officer level. They have sizable staffs, and have complementary advocate offices located at lower echelons throughout the procurement structure of the DoD.

The power of these advocates is best reflected in comments by the Commander of the AF Systems Command in July of this year. "In AFSC my competition advocate reports directly to me about how well we're doing. My program and contracting experts know there had better be a good reason not to compete."

The Streamlining Advocates were established in the Services at flag officer or equivalent level to attack the problem of too many specifications or standards being applied to systems procurement. We in industry fully support the thrust of this effort. We do question, however, the attack on these kinds of problems through the increasing use of advocates. If an advocate, always seemingly at high rank, is appointed for each and every issue that arises, the system will soon become top-heavy with high level officials, each emphasizing his own narrow area of responsibility. Such a management structure could not function in an efficient and effective manner.

In summary, the increasing use of "advocates" to solve individual procurement problems will serve to diffuse responsibilities and to increase confusion among government and industry procurement personnel. The authority of the contracting officer has been diluted by the appointment of advocates with responsibilities which overlap those traditionally assigned to him. (The assignment to the Defense Contract Audit Agency of responsibility for the approval of contractor overhead costs is another dilution of the contracting officer's authority.) As Government Executive magazine recently stated: "The most confused, complex, costly, time-consuming, politicized Federal function is its procurement process." Considering this basically accurate description of the process, those who are involved in its day-to-day operation need more efforts to clarify and simplify the responsibilities of such key officials as the contracting officer. Recent actions by the legislative and executive branches have served to make those efforts increaingly impossible.

b. Applicable Statute or Regulation

(1) Small Business Legislation, 1947 through 1984. (Small Business Representative)

(2) Defense Procurement Bill, FY 1984, Section 403. (Breakout Procurement Center Representative)

(3) The Competition In Contracting Act of 1984 (Competition Advocates)

(4) Deputy Secretary Defense Memorandum to Service Secretaries, 5 Dec. 1984 (Streamlining Advocate)

c. Action Needed

The Congress and the DoD should reconsider their recent efforts to meet procurement management issues through creation of "advocate" positions with authority to question or reverse decisions by responsible procurement authorities. The contracting officer's responsibilities should be analyzed to determine if he still retains sufficient authority to make final contracting decisions in an effective and timely manner.

The Congress should reevaluate those socio-economic programs which affect the procurement process to determine if they are cost-effective, particularly at this time when extraordinary actions must be taken to reduce the over-all cost of the Federal government.

14. Statutes and Regulations which Result in Reduction of the Contracting Officer's Authority

a. Problem

By law, by regulation and by established custom and practice, the contracting officer is the only official who has authority to act as a contracting agent of a procurement organization in the Executive Branch. The contract auditor is one of his advisers, along with advisers in other professional fields involved in procurement: lawyers, scientists, engineers, technicians, industrial and pricing specialists and business analysts. The list is not exhaustive, but it makes the point that a contracting officer is the responsible head of a team.

Many years of experience have shown that there must be a single, responsible official who has a complete overview of the contracting function. The individual members of the team make important contributions, in their areas of expertise, but they cannot be in charge, or held accountable for final contracting decisions.

The 1972 Report of the Commission on Government Procurement reemphasized this conclusion.

Since that time there have been repeated attacks on the authority of the contracting officer. Congress has insisted on diluting this authority by creating an Inspector General office in the DoD, and especially by giving more responsibility to the auditors. Indeed, recent legislation has put the DCAA in charge of final overhead cost determinations.

These decision will lead to increased litigation and have already added to increasing administrative leadtimes.

b. Applicable Statute or Regulation

DoDI 7640.2

Public Law 98-525, Warranties

Deputy Secretary of Defense memorandum, Subject: Audit Determination of Indirect Cost Rates, Dated 5 August 1986

c. Action Needed

The Congress should recommend that the Secretary of Defense withdraw DoDI 7640.2 as it has eroded contracting officers' authorities, lengthened the administrative process of negotiating pricing and accounting issues, and has made no worthwhile contribution to the quality of contracting officers' performance.

The Congress should repeal its requirement for a report from DoD as contained in Public Law 98-525. This law allows the waiver of warranties if they are not cost effective but requires that each waiver be reported to both Armed Services Committees. With each decision subject to critical review by Congress, no waivers are being granted, whether or not the cost-effectiveness can be demonstrated. The contracting officer should have the flexibility to negotiate the best contract for the government, whether it includes warranty coverage or not.

The Congress should recommend that the Deputy Secretary of Defense rescind his memorandum of August 5, 1985. The contract auditor should not have the authority to dictate allowability of costs without benefit of the fact-finding and negotiation process that previously existed with the contracting officer. (Refer to comments on DoD Policy and Regulation on Audit Determinations).

15. Implementing Regulations Reducing the Effectiveness of the Industrial Modernization Incentive Program (IMIP)

a. Problem

This program was initially established to "help focus contractor resources on industrial modernization for the development of more cost efficient production capability for quality weapon systems, equipment," and defense materiel. This basic idea is excellent. This concept is to offer incentives to industry for improving the defense industrial base, based on a structured analysis and implemented through a business agreement to increase use of manufacturing technology, modernization, and engineering/management applications.

In its report dated September 6, 1985, "DOD's Industrial Modernization Incentives Program: An Evolving Program Needing Policy and Management Improvement", the GAO recommended that DOD establish an improved cost and benefit reporting system. The purpose of such a system would be to better quantify IMIP benefits, incorporate them into weapon systems budgets and use them to establish better program cost-effectivety. Benefits are to be quantified and reported "consistently."

DOD concurs in these GAO recommendations.

Industry views these "fine tuning" efforts as reflective of a "bean counting" approach to implementation of what is essentially a very good concept. Cognizant DCAA offices have issued letters of potential con-compliance of CAS 402 in relation to implementing IMIP. Although the DOD policy was designed to allow Service flexibility in its implementation, the pressure of the GAO recommendations and the DOD implementing instructions is acting to stifle the initial motivational thrust toward innovative modernization of the defense industrial base.

b. Applicable Statute or Regulation

DoD 5025.1, October 16, 1980

DoD FAR Supplement Section 15.872,
"Industrial Modernization Incentives"
DoD Instruction 4100.15 "Manufacturing
Technology Program", May 14, 1985

c. Action Needed

The Congress should recommend that the Secretary of Defense take action to resolve the problem of potential noncompliance and/or violation of CAS 402 in relation to implementation of IMIP.

The Congress should recommend that Military Services implementing instructions be reviewed to assure that they are not overly restrictive.

The Congress should recommend that the Secretary of Defense assure that treatment of the requirement for validation of IMIP benefits is consistent in scope throughout the Federal Acquisition Regulation, the IMIP Directive, and the IMIP Guide.

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President

The Honorable William H. Taft IV
Deputy Secretary of Defense
The Pentagon, Room 3E944
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Dear Mr. Taft:

The National Security Industrial Association (NSIA) is a not-for-profit, non-political association of some four hundred industrial, research, legal and educational organizations of all sizes and from all segments of industry interested in and related to the nation's security. For forty-one years its essential purpose has been to foster an effective working relationship and good two-way communication between Government and the industry which provides its defense materiel needs, in the interest of national security.

Member companies of NSIA are increasingly concerned with Navy attempts to force contractors to bear the cost of Special Tooling and Test Equipment (STTE) through depreciation or amortization rather than as a cost of the instant contract -- as STTE has traditionally been costed and priced in accordance with FAR and CAS.

The Navy initiative is predicated on a stated belief that they are merely emulating standard commercial pricing practices. An attempt to justify present thrusts as emulating commercial practices is misleading. Standard commercial pricing practices raise all sorts of issues such as title, joint ownership, competition, etc. We recommend that amortization of STTE be settled on the merits of prescribed Government accounting, costing and pricing policy as opposed to inapplicable references to commercial practices.

This association believes that "special" items of tooling and test equipment should be funded on the initial production contract. It has long been the policy and practice of the DoD to insist that the contractor furnish the required funds to procure all necessary capital equipment (i.e., general purpose) to perform the subject contract(s), but DoD has, additionally, recognized that on most major procurements of hardware there is a category of items which is "special" in that, "without substantial modification or alteration, their use is limited to development of production or particular supplies or parts thereof." When such "special" items of tooling or test equipment are agreed upon to be necessary, the DoD has properly recognized the cost of such STTE as a direct contract cost within the instant contract. The requirement to properly match costs to contracts is similar to your policy statement to the Under Secretary of Defense for Research and Engineering, dated 29 March 1985, concerning the direct charge of proposal costs on sole source follow on contracts.

Attachment 1

The Navy pronouncements to date are difficult to interpret in that accounting terms such as depreciation and amortization are tossed about indiscriminately. On the one hand, if the Navy truly intends to force Navy contractors to capitalize and depreciate (through general overhead) the cost of the Navy's special tooling and test equipment, we object on the basis that (i) special tooling and test equipment is not general purpose and, therefore, should not be capitalized and depreciated; (ii) STTE fails the CAS Part 400 definition of an indirect cost because the subject STTE can be identified with a single final cost objective; (iii) capitalizing and depreciating Navy STTE violates FAR 31-202 and 203 definitions of direct and indirect cost; and, (iv) it is patently unfair (if not illegal) to assign (allocate) to Air Force and Army contracts cost originating specially for Navy contracts.

On the other hand, if it is the Navy's intention to force contractors to amortize this year's cost of STTE over subsequent years annual buys, we object for the following reasons:

1. To amortize STTE does not properly state the cost of the current contract.

Special tooling and test equipment required to execute the instant contract has traditionally been paid for under the instant contract -- the theory being that the instant contract "caused" the cost to be incurred. An argument can be made that subsequent years' production runs "benefit" from STTE; however, the overriding factor, in the past, has been the "causal" effect of the STTE.

2. To amortize STTE creates an awkward indemnification procedure.

The contractor has no control over market planning, product life, financial planning, pricing methodology, intellectual property, competition activities such as dual sourcing, leader follower, or other Government restrictions on a contractor's normal pratices in the commercial marketplace. Therefore, if the contractor is not going to be fully funded under the instant contract for the subject STTE, then he must be funded under subsequent years' buys. If the subsequent years' buys are not part of a multiyear program, then the contractor requires financial protection in the event DoD does not fund the subsequent buy. For the Government to use its monopsonistic power in a competitive fixed-price situation to compel a contractor to accept such financial risk without such protection is unreasonable and blatantly unfair. Therefore, the contractor should be provided with an indemnification clause which protects the contractor from any reduction in planned quantities. The Congress has traditionally asked to be notified of any such indemnification procedures, and would, therefore, need to be involved in each deferral of payment for STTE. Such indemnification without the appropriate reviews and approvals would raise serious concerns with the Services' compliance with Anti-Deficiency laws.

3. Total Program Cost Would Increase.

The policy would entitle contractors to a fair and reasonable return on their investment in unamortized STTE costs. This return would, at a minimum, cover the cost of money to the contractor. As the cost of money is higher for contractors than the Government, the policy would increase total program costs. The current practice is the lowest cost way to finance STTE.

Attachment 1

4. To amortize STTE will reduce competition in the defense industry.

Every contractor is operating with a limited amount of capital to invest at any given time. The requirement to invest in STTE directly reduces the contractor's ability to invest in capital equipment to improve productivity and increase capacity, and would, no doubt, divert the application of resources to the DoD-wide Industrial Modernization Improvement Plan (IMIP). The reduced capital investment will also reduce the surge and mobilization capability, another goal of IMIP. The Navy's desire to transfer funding of STTE from the Government to the private sector will undoubtedly reduce competition and it is questionable whether adequate borrowing capacity exists within the private sector.

The current Navy policy as written is of serious concern to NSIA. In addition, illustrating points made above, interpretation of the policy with respect to STTE by Government contracting personnel creates even more serious problems. A number of Navy contractors are now being presented with demands that they amortize the cost of STTE over several years' production of the end item for which the STTE was designed. They are being told that the Government will give no guarantees that the quantity of items necessary for full amortization will be ordered nor any indemnification for unamortized costs in case the prescribed amortization quantity is not ordered. Also the Government indicates that no allowance for the cost of financing the tooling may be included in the fixed contract price nor will escalation for abnormal inflationary cost increases be allowed. Only the largest or most venturesome contractors could afford to undertake such risks on major programs, and a likely consequence of such terms will be a meaningful reduction in competition for major weapons systems caused by the consolidation of smaller firms into the big ones, serious financial difficulties for some companies and the drop out of others from defense business. Thus we believe the strength of the defense industrial base will be adversely affected.

Conclusion

We recognize that there are now ongoing a proliferation of defense acquisition study initiatives. However, this matter is of such great importance that we strongly recommend that the implementation of this new Navy policy be suspended immediately and that a detailed review be made of the consequences of the policy. It is our firm belief that such a review would show conclusively that the economic assumptions upon which this policy was based are erroneous.

Sincerely,

Wallace H. Robinson, Jr.
President

WHR:ff

Attachment 1

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November 4, 1985

The Honorable William M. Taft IV
Deputy Secretary of Defense
The Pentagon
Room 3E944
Washington, D.C. 20301-1000

Re: Policy Memorandum of Assistant Secretary of the Navy Melvyn R. Paisley on Navy Research and Development Acquisition, September 9, 1985

Dear Mr. Secretary:

I have had an opportunity to review in detail the referenced policy memorandum issued by Assistant Secretary Paisley. The memorandum raises at least three serious problems which I wish to address. In these three cases, the Navy's policy may violate laws, regulations, existing Department of Defense policies, or would cause the Department to regress to acquisition strategies which have previously failed.

The three issues which I believe are raised by the policy memorandum are as follows:

1. the continuing use of competition through Full Scale Engineering Development (FSED) and production;

Attachment 2

2. the use of firm fixed price contracts from the FSED point in a program; and

3. the requirement for assumption of cost risk by contractors for production tooling and Special Test Equipment (STE).

More than any other social or political organization, the Department of Defense seems not to benefit over long periods of time by its experience in procurement management. This may result in part from the changes in personnel which occur cyclically or more often, or from increasing levels of frustration in attempts to control the costs of weapons systems. In all events, the failure to appreciate historical lessons is, in this instance, particularly serious.

A. Competition From FSED

The mandatory nature of Secretary Paisley's policy memorandum with regard to competition, if applied to major weapons systems, could result not in cost savings, time savings and efficiencies, but in greatly increased costs, particularly nonrecurring-type costs, and seriously diluted capacity for sustained production. Efforts of this kind by the Navy to secure second sourcing, some of which are continuing to this date, threaten to undermine the industrial base on which primary production capabilities are now sustained. The idea of institutionalizing such second sourcing techniques is extremely dangerous.

This subject has been addressed on so many occasions that I am amazed at this invocation of second sourcing without any controls, reservations or conditions. As early as 1974, Ron Fox, having recently completed a long tour as Assistant Secretary of the Army and Deputy Assistant Secretary of the Air force, pointed out in his text, Arming America, that the notions of competition which Secretary Paisley is espousing are, for a number of cogent reasons, unworkable. Fox, J. R., Arming America, Harvard University Press (1974) at 467, 471. Subsequently, Jacques Gansler, who may well be the most astute expert on the procurement process, similarly concluded that competition carried on in the manner now made policy by the Navy is unworkable. Gansler, J. S., The Defense Industry, M.I.T. Press (1980) at 29 through 96. Studies performed for the Department of Defense by Rand and L.M.I. have reached similar conclusions. Archibald, Harman et al., Factors Affecting the Use of Competition in Weapons Systems Acquisition, Rand Corp. (1981); Myers, et al., Price Competition in the Department of Defense, L.M.I. (1982). Much more recently, the Comptroller General, in a report to Senator David Pryor, concluded that dual sourcing under circumstances mandated by Secretary Paisley produces no cost or other benefits to the United States. General Accounting Office, "Cost Effectiveness of Dual Sourcing for Production Price Competition is Uncertain," Report B-207152, August 31, 1984.

It is disturbing, to say the least, for the Navy to strike out on its own in this manner when the consequences are so serious, well studied, and conclusively adverse. I question whether it is a prerogative of the Navy to establish such policies, and I suggest that the subject is an appropriate matter for legislative oversight, as well as careful thought within the Department of Defense.

B. The Use of Firm Fixed Price Contracts

Secretary Paisley's policy memorandum mandates the use of firm fixed price contracts "unless the program development risk remains too high." I suggest that FSED is by its nature a process in which development risks are assumed to be too high for fixed price contracting. The Secretary's statement of intent in the policy memorandum is frighteningly reminiscent of a memorandum issued by Secretary Charles in the 1960's which led eventually to the use of total package procurement under DOD Directive 3200.9. It is a known and accepted fact that every program initiated under this Directive failed wholly to achieve cost saving objectives. What is less well understood is the fact that the use of firm fixed price contracting before development and production risks were reasonably fully resolved had a disastrous effect on the defense mobilization base. The negative results of this policy continued for many years after the policy was withdrawn by cancellation of the Directive in 1970.

DOD Directive 3200.9, which established a procurement procedure remarkably similar to that advocated by Secretary Paisley (total package procurement) was cancelled in September of 1970 and replaced by DOD Directive 5000.1. That Directive, most recently amended by your predecessor, Frank Carlucci, in March of 1982, remains in effect to this date. It is my view that Secretary Paisley's policy memorandum directly violates DOD Directive 5000.1, inter alia, because it fails to establish as a requirement the elimination of substantial development, production and cost risks before the initiation of firm fixed price contracting. While it is a seemingly simple matter to cast upon the aerospace and defense industry substantial risks of immature weapons programs, the long term impact on the defense mobilization base must be assessed. This is a process which I believe should be carried on by the Department of Defense (rather than the Navy) in concert with appropriate committees of Congress.

C. Production, Tooling and STE Cost Risks

Secretary Paisley has decreed that "production, tooling and special test equipment investment by contractors is an allowable recoupment only under a competitive RFP bid." This mandate violates a criminal statute, 31 U.S.C. § 1342, numerous DOD Directives, and specific regulations governing the allowability and allocability of contract costs. Of equal seriousness, its imposition could place contractors in the position of having to expense such costs against IR&D, B&P, manufacturing and production engineering, and other categories of cost charging. As you may know, where such practices have been followed in the past, DCAA has taken issue and serious civil and potential criminal questions have been raised.

It is fundamentally contrary to law and established Department of Defense policies to require contractors to assume the risk of recovery of costs incurred in the development and manufacture of special use capital goods. To invoke the policy mandated by Secretary Paisley would require numerous statutory changes and changes in DOD Directives and regulations which can only be made by you. From a purely policy standpoint, it would appear that such changes should not be made because of the improper burdens which it would impose on industry. See Fox, J. R., Revamping the Business of National Defense (1982), Harvard Business Review 5, at 66, 67.

I urge you to direct the suspension or revocation of the subject policy memorandum, at least until its implications can be carefully considered by Congress and the Department of Defense. While I can well appreciate the concerns on which the policy memorandum is based, I believe that careful consideration of the three problems suggested above would indicate that the policy will not accomplish its objectives.

I would, of course, be pleased to discuss this subject with you further at your convenience.

Sincerely,

Herbert L. Fenster

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November 25, 1985

The Honorable William M. Taft IV
Deputy Secretary of Defense
The Pentagon
Room 3E944
Washington, D.C. 20301-1000

Re: Policy Memorandum of Assistant Secretary of the Navy Melvyn R. Paisley on Navy Research and Development Acquisition, September 9, 1985; Secretary of the Navy Instruction 4210, Dated November 20, 1985

Dear Mr. Secretary:

I refer to my letter of November 4, 1985 concerning the captioned policy memorandum. I also refer to the letter of October 29, 1985 from Sanford McDonnell concerning the same subject. In light of the rather serious issues raised in our letters, I had hoped that the Department of Defense would delay any further initiatives on this subject until the matter could be studied carefully and the views of Congress solicited.

On November 20, 1985, the Secretary of the Navy issued the captioned instruction, which not only adopted the initiative but made it mandatory for Navy programs. As you may know, among the Navy's programs which are being made subject to this initiative are several which will affect all three services. Thus, the initiative and the instruction will have substantial application beyond the Navy.

Attachment 3

The Honorable William M. Taft IV
November 25, 1985
Page Two

Mr. McDonnell's letter quite eloquently set forth the reasons why the underlying assumptions of the initiative and the instruction are invalid from a business standpoint. My letter attempted to show that the initiative (and now the instruction) is legally flawed and a rejection of important lessons derived from recent history.

To the foregoing I would add the view that the initiative and the instruction clearly violate the "full funding" policy of Congress. This policy, which is now approximately twenty years old, requires the Executive Branch to seek and obtain from Congress, by appropriation, the funds necessary to perform programs prior to the time when obligations necessitating those funds are incurred. The purpose, of course, is to avoid what is by analogy off balance sheet financing and hidden unbudgeted obligations.

A rough estimate of the programs which the Navy is presently pursuing on this basis indicates that the capital-type funds which may now be subject to the instruction may total as much as $1.5 billion. It is unclear whether appropriated funds have been apportioned, allocated and obligated for these purposes, but it is likely that in substantial measure they have not.

It is extremely unfortunate that the Navy saw fit to impose this ill-considered instruction on the Department of Defense, and it is even more unfortunate that the Department of Defense has permitted the instruction to go into effect without review and consultation with Congress. I believe that the problems raised in Mr. McDonnell's letter and my own should have a full airing, in public, before the extraordinary risks embodied in the instruction are imposed on industry and necessarily Congress. I hope you will consider further this subject and provide clear leadership on it to the defense community.

Sincerely,

Herbert L. Fenster

HLF/gt

Attachment 3

Independent Research and Development Bid and Proposal

1. What is meant by IR&D and B&P?

Independent Research and Development (IR&D) is a term used by the department of Defense (DoD) and Federal agencies to differentiate between a contractor's research and development technical effort performed under a contract, grant, or other arrangement (R&D) and that which is self-initiated and self-funded (IR&D).

Bid and Proposal (B&P) is a term used by DoD and Federal agencies to describe a contractor's technical and supporting effort directed at preparing and submitting proposals (solicited or unsolicited) to a customer to meet an identified customer requirement.

IR&D and B&P exist because private firms doing business with the Government must develop advanced technologies necessary for future products and services (IR&D), and must incur the costs of bidding and proposing these products and services (B&P).

It is important to understand what IR&D and B&P efforts really are, why they are absolutely essential, and how they differ.

IR&D has as its primary characteristic the stimulation of new ideas and concepts for advancing technology and applying these to the solution of current and future problems. These efforts are independently initiated and funded by contractors. These costs are normal costs-of-doing business and are recovered through sales of products or services. B&P is that activity undertaken by a company to respond to specific Government requirements by the application of its particular technological expertise.

2. How are IR&D and B&P costs recovered:

A portion of the costs associated with a contractor's IR&D and B&P efforts is allowable as an indirect cost allocable to his DoD and NASA contracts. Thus, IR&D/B&P is not a program funded by the government. A company, large or small, must win and perform government contracts in order to recover a portion of its IR&D/B&P costs as allowable indirect charges to these contracts, i.e. no contracts, no cost recovery. For the major companies, determination of the portion of a company's IR&D/B&P costs that will thus be allowable is a complex process, as illustrated by the following highlights of the Public Law which governs IR&D/B&P cost-recovery on DoD contracts:

o DoD proposal requirements are dramatically more comprehensive and voluminous than the requirements associated with commercial business. DoD reimburses less than its proportional share of the associated B&P costs.

3. How well do DoD's regulations and control of IR&D/B&P reflect the intent of Public Law?

In the area of IR&D, DoD procedures go far beyond the intent of the Public Law. For example, S.203. Public Law 91-441 requires that:

"The IR&D portions of the advance agreements thus negotiated are based on company submitted plans on each of which a technical evaluation is performed by the DoD prior to or during the fiscal year covered by such advance agreement."

The law does not prescribe a rigid, formulistic scoring of an extensive narrative presentation of each and every project in a major defense contractor's IR&D program. However, DoD has implemented an extensive and very detailed proces for performing this technical evaluation. To illustrate, the technical plans of one major defense contractor which are required each year total 9000 pages per copy, and a total of five tons of his plans were distributed to DoD centers and laboratories for evaluation. This is far from an isolated case.

Analysis has indicated that 5% or more of the IR&D costs to industry represent time spent by the principal investigators, engineers, and scientists in composing their technical material in the format and depth required for the DoD IR&D Technical Plan over and above that time required for normal documentation of technical work. This excessive effort is required, since the Technical Plan must contain sufficient detail to permit unknown evaluators to accord it a representative and fair technical rating solely by reading the submitted material. Removal of this requirement could either reduce costs, or could release the equivalent amount of a scientist's or engineer's time for the address of productive technical work, yielding significant additional IR&D work for the same cost.

In addition to this annual technical plan documentation, the DoD also requires, every three years, an on-site review of the contractors IR&D. This is a extensive evaluation of the already submitted documentation. It normally requires two to three days of presentations involving many man hours of technical time on the part of both the contractor and the government.

Further, for IR&D/B&P costs to be recoverable, the Secretary of Defense must determine that the effort generating such costs has a Potential Relationship to a Military function or operation ("PMR").

This elaborate procedure for determining dollar ceilings for IR&D/B&P costs contrasts sharply with the treatment of all other allowable indirect costs allocable to DoD contracts, subject only to the criterion of "reasonableness." Another striking difference in the treatment of IR&D/B&P costs is a requirement that these overhead costs be further burdened with the appropriate overhead rate (in most cases, this is the company's engineering overhead rate). It is difficult for those unfamiliar with accounting procedures to appreciate the fact that this requirement more than doubles the IR&D/BP costs statistics that are compiled annually and reported to

Congress by DoD. These figues convey a correspondingly erroneous impression of the "cost" of the defense contractors' IR&D/B&P efforts. Were IR&D/B&P activities discontinued completely, more than half of the annually reported costs would still accrue to DoD contracts, since the overhead previously applied to IR&D/B&P costs would now have to be applied to and absorbed by the remaining direct cost elements.

The annually negotiated dollar ceilings for a contractor's IR&D/B&P costs are then pro-rated over his total business base for that year and his DoD contracts are allocated a proportional share of these ceilings. These costs are then allowable, provided that his IR&D/B&P efforts contain a corresponding quantity of work that meets the potential military relationship requirement.

A contractor must recover the remainder of his IR&D/B&P costs by allocating them to his other business (if any) or by suffering a reduction of profits. Thus, these legally-mandated procedures result in a very inequitable situation for DoD:

o DoD technical community has full use of detailed plans of the major defense contractors' total IR&D programs, while paying less than its proportional share of the associated costs. Overall, DoD "pays" only some 30¢ for each $1 of IR&D work.

DoD could perform adequate technical evaluations appropriate to the intent of S203 of Public Law 91-441 by:

o Making the IR&D Data Bank submittals mandatory for all major defense contractors.

o Performing periodic or sampling checks of the continuing technical quality of a contractor's IR&D program by using only IR&D Data Bank information, and using a contractor's existing internal technical reports on selected IR&D projects.

o Modifying the procedures for On-Site Technical reviews, substituting (for the current massive tri-annual reviews of substantial portions of a contractor's IR&D program) annual reviews by small specialist teams. These teams would review selected IR&D projects, based upon DOD's technical interests or concerns resulting from its scrutiny of a contractor's Data Bank submissions.

4. In summary, the best interests of the government and industry would be served by modifying the current procedure for technical evaluations, with its associated proparation and submission of voluminous narrative Technical Plans by defense contractors. Retention of the DoD IR&D/B&P Data Bank coupled with selective access to contractors' internal technical reports on their IR&D projects and "sampling-type" on-site reviews by small specialist teams would afford government reviewers insight regarding the IR&D activities of major defense contractors. This satisfies the intent of P.L. 91-441, at minimal administrative cost, while simultaneously releasing significant engineering and scientific effort to the pursuit of more productive activities.

TABLE 1. SOCIAL AND ECONOMIC PROGRAMS

Program	*Authority*	*Purpose*
Buy American Act*	41 U.S.C. 10a–10d	To provide preference for domestic materials over foreign materials
Preference for United States Manufacturers	22 U.S.C. 295a	To provide preference for domestic manufactures in construction of diplomatic and consular establishments
Preference for United States Manufacturers	16 U.S.C. 580a	To restrict U.S. Forest Service from purchasing twine manufactured from materials of foreign origin
Preference for United States Products (Military Assistance Programs)*	22 U.S.C. 2354(a)	To require the purchase of U.S. end products for the military assistance program
Preference for United States Food, Clothing, and Fibers (Berry Amendment)*	Public Law 91-171, sec. 624	To restrict the Department of Defense from purchasing specified classes of commodities of foreign origin
Officials Not to Benefit*	41 U.S.C. 22	To prohibit members of Congress from benefiting from any Government contract
Clean Air Act of 1970	42 U.S.C. 1857h–4	To prohibit contracting with a company convicted of criminal violation of air pollution standards
Equal Employment Opportunity*	Exec. Order 11246, Exec. Order 11375	To prohibit discrimination in Government contracting
Copeland "Anti-Kickback" Act*	18 U.S.C. 874, 40 U.S.C. 276c	To prohibit kickbacks from employees on public works
Walsh-Healey Act*	41 U.S.C. 35–45	To prescribe minimum wage, hours, age, and working conditions for supply contracts
Davis-Bacon Act*	40 U.S.C. 276a–1–5	To prescribe minimum wages, benefits, and work conditions on construction contracts in excess of $2,000
Service Contract Act of 1965*	41 U.S.C. 351–357	To prescribe wages, fringe benefits, and work conditions for service contracts
Contract Work Hours and Safety Standards Act*	40 U.S.C. 328–332	To prescribe eight-hour day, forty-hour week, and health and safety standards for laborers and mechanics on public works
Fair Labor Standards Act of 1938	29 U.S.C. 201–219	To establish minimum wage and maximum hours standards for employees engaged in commerce or the production of goods for commerce
Prohibition of Construction of Naval Vessels in Foreign Shipyards	Public Law 91-171 (DOD Appropriation Act of 1970), title IV	To prohibit use of appropriated funds for the construction of any Navy vessel in foreign shipyards
Acquisition of Foreign Buses	Public Law 90-500, (DOD Appropriation Act of 1969), sec. 404	To restrict use of appropriated funds to purchase, lease, rent, or otherwise acquire foreign-manufactured buses
Release of Product Information to Consumers	Exec. Order 11566	To encourage dissemination of Government documents containing product information of possible use to consumers
Prohibition of Price Differential	Public Law 89-179, sec. 644	To prohibit use of appropriated funds for payment of price differential on contracts made to relieve economic dislocation
Required Source for Jewel Bearings*	ASPR 7-104.37	To preserve a mobilization base for manufacture of jewel bearings

Program	*Authority*	*Purpose*
Employment Openings for Veterans*	Exec. Order 11598, 41 CFR 50-250, ASPR 12-1102	To require contractors to list suitable employment openings with State employment system to assist veterans in obtaining jobs
Covenant Against Contingent Fees*	41 CFR 1-1.500-509	To void contract obtained by broker for a contingent fee
Gratuities*	32 CFR 7.104-16	To provide Government with right to terminate if gratuity is given to a Government employee to obtain contract or favorable treatment
International Balance of Payment*	ASPR 6-805.2, FPR 1-6.8	To limit purchase of foreign end products and services for use abroad
Prison-made Supplies	18 U.S.C. 4124	To require mandatory purchase of specific supplies from Federal Prison Industries, Inc.
Preference to U.S. Vessels*	10 U.S.C. 2631, 46 U.S.C. 1241	To require the shipment of all military and at least half of other goods in U.S. vessels
Care of Laboratory Animals*	ASPR 7-303.44	To require humane treatment in use of experimental or laboratory animals
Required Source for Aluminum Ingot*	ASPR 1-327, FPR subpart 1-5.10	To eliminate excess quantity of aluminum in the national stockpile
Small Business Act*	15 U.S.C. 631-647; see also 41 U.S.C. 252(b) and 10 U.S.C. 2301	To place fair portion of Government purchases and contracts with small business concerns
Blind-made Products	41 U.S.C. 46-48	To make mandatory purchase of products made by blind and other handicapped persons
Duty-free Entry of Canadian Supplies*	ASPR 6-605	To further economic cooperation with Canada and continental defense
Use of Excess and Near Excess Currency*	ASPR 6-000 et seq., FPR 1-6.804-806	To provide preference in award to bidders willing to be paid in excess or near-excess foreign currency
Purchases in Communist Areas*	ASPR 6-401 et seq.	To prohibit acquisition of supplies from sources within Communist areas
Nonuse of Foreign Flag Vessels Engaged in Cuban and North Vietnam Trade*	ASPR 1-1410	To prohibit contractor from shipping any supplies on foreign flag vessel that has called on Cuban or North Vietnamese port after specific dates
Labor Surplus Area Concerns*	Defense Manpower Policy No. 4, 32A CFR 33 (Supp. 1972)	To provide preference to concerns performing in areas of concentrated unemployment or underemployment
Economic Stabilization Act of 1970	12 U.S.C. 1904 note	To stabilize prices, rents, wages, salaries, dividends, and interest
Humane Slaughter Act*	7 U.S.C. 1901-1906	To purchase meat only from suppliers who conform to humane slaughter standards
Miller Act*	40 U.S.C. 270a-d	To require contractor to provide payment and performance bonds on Government construction contracts
Convict Labor Act*	Exec. Order 325A, ASPR 12-201 et seq.	To prohibit employment on Government contracts of persons imprisoned at hard labor
Vietnam Veterans Readjustment Act	Public Law 92-540	To give employment preference to disabled veterans and veterans of the Vietnam era

*Indicates that the program has resulted in the issuance of a standard contract clause
Source: Commission Studies Program.

Attachment 5

TABLE 2. SUMMARY OF PROBLEMS ASSOCIATED WITH SOCIAL AND ECONOMIC PROGRAMS

Act	*Original enactment date*	*Agencies sharing responsibility with procuring activity*	*Problems*
Davis-Bacon Act (40 U.S.C. 276a-1 to 276a-5)	1931	Department of Labor; Comptroller General	● Low dollar threshold. ● Ambiguity or lack of definition of important terms, including "site of work," "public work," "construction, alteration, or repair" versus "maintenance." ● Ambiguity of enforcement responsibility. ● Improper determinations of prevailing wage rates. ● Excessive reporting requirements.
Walsh-Healey Public Contracts Act (41 U.S.C. 35–45)	1936	Department of Labor; Comptroller General	● No wage determinations made since 1964. ● Fair Labor Standards Act of 1938 and Occupational Safety and Health Act of 1970 overlap and make much of act unnecessary. ● Inhibition of use of 4-day, 10-hour work week. ● Prohibition of use of convict labor is contrary to current rehabilitation policies.
Copeland "Anti-Kickback" Act (18 U.S.C. 874 and 40 U.S.C. 276c)	1934	Department of Labor	● Reports required cause administrative burdens. Total impact minor.
Miller Act (40 U.S.C. 270a–d)	1935	Comptroller General	● Unrealistically low dollar threshold. ● Technically qualified small contractors, including minority contractors, may have equipment, expertise, and desire to perform but lack credit rating sufficient to be bondable. ● Bonding costs to Government are substantial. ● Nonuniform practices as to (a) whether agencies may waive bonding requirement for cost-type contractors, and (b) requiring bonds from fixed-price subcontractors of cost-type prime contractors.
Buy American Act (41 U.S.C. 10a–d)	1933		● Nonuniform regulations and procedures make administration of act confusing to suppliers. ● Definition of "domestic" allows inclusion of up to 50 percent of foreign components (by cost) in a domestic end product and makes purchase of foreign components (only) as replacement parts difficult. ● Suppliers' certifications of percentage of foreign components in an end product are difficult for procurement personnel to verify. ● Act applies to all contracts regardless of amount.
Convict Labor (Executive Order 325A)	1905		● Changing attitudes in rehabilitation programs cast doubt on currency of law, particularly since

Attachment 5

Act	*Original enactment date*	*Agencies sharing responsibility with procuring activity*	*Problems*
			under another statute Federal prisoners may work for pay in local communities under work release programs.
Labor Surplus (Defense Manpower Policy No. 4)	1952	Office of Emergency Preparedness; Department of Labor	● Prohibition against payment of price differentials for award to labor surplus area concerns prohibits total set-asides and complicates procedures. ● Program conflicts with small business program.
Equal Opportunity (Executive Order 11246)	1965	Department of Labor (Office of Federal Contract Compliance); Designated "Compliance Agencies"	● Contractor may be subject to review by several compliance agencies, particularly when he operates in more than one industry. ● Complaint may result in contractor being investigated both by OFCC and EEOC for the same alleged violation. ● Pre-award solicitations and requirements are numerous, confusing, and cause delay.
Service Contract Act (41 U.S.C. 351–357)	1965	Department of Labor; Comptroller General	● Wage determinations are often improperly made by using "median rates or slotted rates" as prevailing rates. ● The act is often extended to cover professional engineering and technical employees although it applies only to service employees. ● Rates applicable to the area of the procuring activity are applied if the place of performance is unknown. ● Recent amendments may reduce competition between potential service contractors and have an inflationary effect. ● Even the unrealistically low $2,500 threshold for wage determinations appears to have been eliminated by recent amendments.

Source: Commission Studies Program.

Attachment 5

STREAMLINE AND ELIMINATE SPECIFICATIONS AND REQUIREMENTS

Nearly every broad-based study of defense business has been critical of the great number and excessively detailed contents of specifications imposed on defense programs. This condition is present 'from cradle to grave': at the inception of new systems and throughout the whole range of procurement activity.

We will approach the problem of excessive specifications from the perspective of major defense systems development and production. Most major systems include System Specifications containing system requirements; Critical Item Specifications containing component requirements (Part I - for performance and design - and Part II - for fully-detailed description (build-to-documentation)); and, many levels of Military Standards and Military Specifications containing equipment, assembly, fabrication processes, material processes and testing requirements.

There are over 40,000 Military Standards (Mil-standards) and Military Specifications (Mil-specs) applicable to defense contracts. Many specify technical characteristics of products. Many other types of mil-specs and mil-standards contain specific ("how to") procedures as opposed to general or objective criteria. There is a need for all Mil-specs and Mil-standards to be periodically reviewed to determine if they are relevant and necessary and, if not, to be tailored or dropped. The kind and coverage of reviews which are needed to keep specs and standards current and to prevent them from becoming counter-productive are not occurring.

A "how to" requirement is becoming more prevalent in Mil-standards and Mil-specs. This characteristic of defense procurement threatens industry's ability to develop cost effective solutions to the functional and operational performance requirements of weapons systems. Ways need to be found to validate and monitor contractors' existing management systems without forcing more and more administrative burdens on contractors by incorporating Mil-specs and Mil-standards into contracts, requiring contractors to change their systems to conform to detailed, government-specified procedures. Finally, there is a strong push within the defense agencies for full and literal compliance with all government-specified procedures, and also for something beyond: for government direct control over the workplace, the workforce and contractor management.

This paper will develop the above points and recommend actions which we believe would improve the productivity of resources involved in defense contracting.

Technical Currency and Tailoring

Although a DOD Directive (4120.21), dated 7 April 1977 and provided as Attachment A, requires procurement agencies to tailor specifications and standards to meet the specific requirements of products, it remains the prevailing practice to incorporate them -- and by references in them, a large

Attachment 6

group of other specifications and standards -- into contracts without clarification or limitation (See Attachment B).

These specifications and standards should be periodically evaluated to determine if they are current and relevant and, when found not to be, to be updated and/or tailored before they become contractual obligations.

Typically, this does not happen. The failure of any effective implementation of the 1977 DOD Directive results in contracts which become obstacles to efficient work performance. If not technologically current and if not tailored to the relevant conditions of the modern, competitive industries which develop and produce advanced technological products, Mil-standards and Mil-specs can prevent contractors from following their existing and workable procedures, require contractors to adopt internal management procedures that are obsolete, unnecessary or inappropriate and require contractors to pursue costly, cumbersome and disruptive contract deviation procedures in order to avoid obvious waste.

Tailoring should be pursued to accomplish four desirable objectives:

Direct Cost Reduction: Relaxation or deletion of requirements that are not technical needs of the particular hardware or weapons system.

Clarification of the Requirements: Clarification of requirements that are stated in such a way that the intent, measurement method or limit is ambiguous, ambivalent, vague or contradictory.

Requirements Standardization: Resolution and revision of requirements that overlap and differ from other required military standards or specifications without technical justification.

Technology Updating: Revising obsolete requirements and methods to reflect or allow improvements in materials, processes and techniques that take advantage of new technology.

Elimination of Excessive Specifications

Many specifications, over time, have become unnecessarily excessive and thereby require elimination. The following two instances are examples of such:

a. Critical Item Specifications - Part I - Should be Eliminated After Functional Configuration Audit

As noted above, Critical Item Specifications - Part I - contain descriptions of component requirements of a military system. After successful completion of Functional Configuration Audit (FCA), which demonstrates that the Part I specs have fulfilled their purpose, the maintenance of Part I Critical Item Specifications should be discontinued. The contractor should thereafter be allowed to use his manufacturing drawings, process specifications, and acceptance test procedures to do the job. This would eliminate a great deal of documentation that really is no longer used by the contractor, or necessary for proper contract management and performance. Curtailing paperwork systems and placing greater reliance on the exercise of sound and informed judgment is no longer permitted in the current criticism-dominated climate. The unnecessary cost is high and continuous and the requirement to follow unproductive procedures is demoralizing.

b. The Creation and Maintenance of Critical Item Specifications - Part II - Should be Discontinued

The Part II Configuration Item/Critical Item Product Fabrication Specification should be eliminated as a contract requirement for development and production of military systems. The basic function of these specifications (which define "build to" requirements) is performed adequately by contractor drawings and acceptance test procedures. Large volumes of documentation requiring a great deal of expensive engineering time and talent could be eliminated and the associated costs of the preparation, review, and approval cycles for both industry and government agencies significantly reduced. Part number control (as opposed to specification control) is a normal practice by all defense procurement agencies. Specification control is not practiced by the agencies as the method of maintaining control over the configuration of the contract end items. Configuration control is the real need and objective. Thus, the expensive specification preparation, review, approval and maintenance is a lot of costly work that doesn't have to be done in order to meet the real need and objective.

Elimination of the Part II specs would require no change in normal practice after establishment of the product configuration at Physical Configuration Audit. It used to work very well in defense production and it still can. It works very well in commercial production. This recommendation would eliminate jobs in government and industry. This is its principal drawback.

The "How To" Requirement

In recent years, a strong trend has developed, and is accelerating, to extend the content of Mil-specs and Mil-standards from "what" must be done to meet the desired requirements, to "how to" do it and even "when" and with "what". Examples of this are the recent unilateral* changes by defense procurement agencies to MIL-Q-9858A and MIL-STD-1520B. Both changes relate to the collection and reporting of various elements of Quality Assurance costs, particularly costs associated with Scrap, Rework and Replacement (SR&R). Combined, both changes are very specific in the how, what, when and itemization pertaining to data collection, coupled with the imposition of highly subjective criteria.

There are real dangers in this increasing "how to" trend in specifications. It acts to constrain and reduce substantially the ability of contractors to develop and employ advanced, technologically innovative and cost-effective solutions to the functional and operational performance requirements of weapon systems. Industry and government representatives find themselves allocating more and more time, expensively, to overly detailed control systems and procedures and to voluminously reporting on all aspects of the government-directed methods, creating data for government use which contractors in general do not consider necessary or productive, instead of to developing, selecting and improving the best methods available to meet weapon system needs.

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* (Defense procurement agencies are requiring contractual acceptance of both revisions by individual agency action, circumventing the established Mil-spec revision process.)

The "how to" methodology engenders standardization and uniformity. This drives contractors to a point of total compliance and therefore of diminished competitiveness. The proof of this statement is the virtually complete absence of such methodologies in commercial development and production. The competitive edge is derived painstakingly from trial, error and newly discovered and developed methods. The government gains economic or technical advantages from such advances. To write such "how to" data into the specifications only serves to freeze into place requirements for contractors to use methodologies which inevitably will become outdated, ineffective and counter-productive. This is especially true in defense contracting, because of the absence of any workable system which purges and replaces spec contents.

It is therefore recommended that the content of Mil-specs and Mil-standards be reviewed with the intent to eliminate unnecessarily restrictive and technically or economically unjustifiable requirements. Those that are essential should be expressed only in terms of general criteria and never in "how to" procedures.

Additionally, and most importantly, a "sunset" date should be established for all Military Standards and Specifications whereby they are automatically rescinded if not reviewed and updated prior to the established date in a publicly conducted process. As the particular specification draws near time of expiration, the Government should solicit public comments for continuation, modification, or elimination of the Mil-standards and Mil-specs and follow the review process rigorously. Publication of rationale for changes and for the treatment of public comments should be mandatory.

Validate and Monitor Existing Manufacturing and Quality Systems

The chart provided as Attachment C shows the growth in directed Quality Assurance tasks over the last 40 years. Similar charts could be developed for engineering, manufacturing, financial, and purchasing functions. Many of the requirements shown as being added since the 1940's were originated and performed over the years by contractors using internal methods and procedures. However, as Military Standards and Specifications grew and new government regulations and directives were issued, industry-wide compliance was "institutionalized" and the methods and procedures were required to be measured in a specified manner with associated reviews and paperwork.

Some way must be found to break this self-nourishing spiral of government control and intrusion into the province of private sector management. The Defense Department's only real need is to review and validate a contractor's existing operating systems so as to verify its intent, content and workability. Qualified Government personnel could then monitor the operation and results of the approved system. This approach is currently used by the FAA in validating commercial aircraft development and production and, to some extent, for DOD-required Cost/Schedule Control Systems (C/SCS). Government has a voracious appetite for specific methodology and for a multitude of requirements. An appetite does not constitute a need. Often the opposite is the case. Defense contracting is such a case.

CONCLUSION

The proliferation of Military Specifications and Military Standards and their blanket, indiscriminate application to weapon system acquisition is a needless extravagance, is self-perpetuating and is much more costly than its benefits warrant. We recommend that the Commission pursue or prescribe independent assessment of the progress made on the DOD acquisition "Streamlining" program promulgated by Secretary Taft (Attachment D) and offer recommendations which would help assure the attainment of the widely acclaimed objectives of the DOD streamlining initiatives, recognizing that attainment of these objectives would require a cultural revolution, and that this is never easily or readily attainable.

ATTACHMENTS A THROUGH D

Attachment 6

ATTACHMENT A

April 9, 1977
NUMBER 4120.21

ASD(I&L)

Department of Defense Directive

SUBJECT Specifications and Standards Application

References: (a) DoD Directive 5000.19, "Policies for the Management and Control of Information Requirements," March 12, 1976
(b) DoD Directive 4105.62, "Selection of Contractual Sources for Major Defense Systems," January 6, 1976
(c) Armed Services Procurement Regulations
(d) DoD Directive 5000.1, " Major System Acquisitions," January 18, 1977
(e) Deputy Secretary of Defense Memorandum to Secretaries of the Military Departments, "Specifications and Standards Application," August 4, 1975 (hereby cancelled)

I. PURPOSE

This Directive establishes the policies and procedures governing the application and tailoring of specifications and standards to achieve cost-effective acquisition and life cycle ownership of defense materiel.

II. APPLICABILITY AND SCOPE

The provisions of this Directive apply to the Military Departments and the Defense Agencies (hereinafter referred to collectively as "DoD Components") in the application and tailoring of specifications and standards in materiel acquisition.

III. DEFINITIONS

As used herein, the following definitions apply:

A. Application. The orderly process of reviewing and selecting from the total realm of available specifications and standards those that are considered to have

Continuation of III.A.

application to the particular materiel acquisition program and contractually invoking these wholly, or in part, at the most advantageous status point in the system development cycle.

B. Tailoring. The process by which the individual requirements (sections, paragraphs, or sentences) of the selected specifications and standards are evaluated to determine the extent to which each requirement is most suitable for a specific materiel acquisition and the modification of these requirements, where necessary, to assure that each tailored document invoked states only the minimum needs of the Government.

C. Review Board. A board established within the various levels of DoD Component organizations for the purpose of (1) performing one or more management functions, such as reviewing proposed solicitations and/or model contracts for consistency with law, policy regulations and direction from higher authority; (2) reviewing proposed specifications and standards to assure conformance to policy and operational need; or (3) reviewing data requirements for conformance to policy and minimum need. Makeup of the board may vary depending upon the acquisition value, complexity, and status of the program to be considered.

IV. OBJECTIVE

A. The objective of this Directive is to make all levels of management aware of the need to assure more cost-effective utilization of specifications and standards in materiel acquisition; that specifications and standards are susceptible to selective application and tailoring to a particular program; and that these documents must be applied and tailored by giving due consideration to required performance versus costs and achievement of minimum required operational needs. The technique of application and tailoring of specifications and standards is discussed further in enclosure 1.

B. The misapplication and insufficient tailoring of specifications and standards in defense acquisition programs sometimes has led to increased costs and delays in the introduction of new hardware. This can be attributed to past emphasis on achieving maximum performance without regard to cost, to the institutionalized attitude that specifications and standards were mandatory and had to be applied in their entirety, and to the lack of emphasis on the proper application and tailoring of documents to a specific need.

V. POLICY

The following shall govern the application and tailoring process, as conducted by the DoD Components:

A. Specifications and standards used in acquisition programs

Continuation of V.A.

shall be selectively applied and tailored to impose the minimum essential system needs.

B. Data requirements to be imposed in acquisition programs shall be consistent with the tailored requirements imposed by the governing specifications and standards and the policies enunciated in DoD Directive 5000.19 (reference (a)).

C. The blanket contractual imposition of specifications and standards in acquisition programs shall be avoided and controlled to the maximum practical extent.

D. A management review board shall examine all acquisition programs to assure that the specifications, standards and Data Item Descriptions used have been tailored.

E. The results of the document application and tailoring process shall be made a matter of permanent record, certified and made available to the review board.

F. When consistent with the proposed procurement method (such as prescribed in DoD Directive 4105.62, reference (b), and Section II, Part 5 of the Armed Services Procurement Regulations, reference (c)), recommendations or comments shall be solicited from prospective contractors during the acquisition process to determine whether additional cost-effective application and tailoring of cited specifications and standards can be accomplished, or cost-effective substitutions proposed.

VI. RESPONSIBILITIES

DoD Components shall:

A. Establish specific, continuing, management controls over the utilization of specifications, standards and, pursuant to the provisions of DoD Directive 5000.19 (reference (a)), Data Item Descriptions in the acquisition process to assure that these documents have been properly applied and tailored to reflect the minimal essential requirements for the particular system.

B. Institute procedures and policies to control blanket contractual imposition of specifications and standards in acquisition programs.

C. Establish procedures to assure that Data Item Descriptions used in acquisition programs do not reimpose requirements eliminated through the process of tailoring the source document.

Continuation of VI.

D. Establish procedures to provide feedback from prospective contractors during the acquisition process. Beneficial recommendations from prospective contractors shall be solicited to determine whether additional cost-effective application and tailoring of cited specifications, standards and data requirements can be accomplished, or cost-effective substitutions proposed. Responsibility for review of such comments shall be specifically assigned. These proposals shall receive full consideration based upon thorough technical analysis.

E. Establish and maintain records for each acquisition program to record the extent to which specifications, standards and Data Item Descriptions have been applied and tailored. As a minimum, the record shall list those specifications, standards and Data Item Descriptions which are cited by number in the Statement of Work and system/contract specifications and the manner and degree in which they have been tailored. Enclosure 2 illustrates the type of information to be included in these records, which shall be part of a permanent file.

F. Assure that functional technical groups involved in the acquisition process are made fully aware of these policies; that they structure system/equipment requirements in a manner consistent with these principles and that they impose only those requirements which are essential to specific operational needs of the end item, equipment or system.

1. Functional technical groups who are responsible for imposing particular requirements including disciplines such as reliability, maintainability, configuration management, quality, safety, and human factors shall tailor the application of these requirements to the specific acquisition program.

2. Such tailoring must commence at the earliest possible time in the acquisition process and must include the participation and cooperation of all personnel in a concerted effort to avoid unnecessary, costly requirements that offer only marginal contributions to system effectiveness.

3. Procedures shall be established to require a formal certification from the proponent that the requirement to be imposed has been reviewed, evaluated and tailored, and represents the minimum essential need for that system. This certification shall be retained as a matter of record.

Continuation of VI.

G. Assign specific responsibility to an existing management review board (e.g., Acquisition, Solicitation, Specification, or Data Requirements Review Board) for:

1. Reviewing, evaluating, and approving the extent and degree of tailoring that has been accomplished. In most cases, such boards will not normally perform the tailoring process themselves. It must be accomplished by the functional technical groups early in the program. The board will determine the extent of tailoring and verify the fact that it was accomplished by a review of the records required to be maintained under the provisions of VI.E.

2. Ensuring that solicitations include provisions for obtaining feedback from prospective contractors regarding further cost-effective application and tailoring of cited specifications, standards, and data requirements.

3. Assuring that all comments from prospective contractors have been reviewed and evaluated for use in the procurement.

H. Pursuant to DoD Directive 5000.1 (reference (d)), assign specific responsibility to Program Managers for assuring that all requirements imposed upon their system (such as operational characteristics, specifications, standards, and data) have been properly applied and tailored and are the minimum consistent with stated need; that all such requirements are challenged; and are justified by the proponent. For major programs, the Program Manager shall document the degree of tailoring accomplished and the impact on performance, schedule, and cost at the time of DSARC review. A brief summary shall also be included in the Decision Coordinating Paper (DCP). System specifications and statements of work shall be developed in coordination with functional technical groups and shall be in consonance with the policies prescribed herein. In the case of systems or programs that are of interest to more than one Service, the Program Manager must assure that each Service's essential needs are met during the tailoring process. This is particularly true in matters such as operational requirements, system interface, interoperability, and logistics support.

I. Document the experience gained in the use of the procedures established by this Directive. This information will be evaluated by the staff of the Assistant Secretary of Defense (Installations and Logistics) during the course of their review and discussions with the DoD Components in monitoring the implementation and effectiveness of this Directive.

VII. REQUIREMENTS

The continuing effort to fully integrate these policies into the materiel acquisition process will require numerous actions at the Service level. Among these, consideration should be given to the following:

A. Review and adopt necessary revisions to internal guidance documents, such as "Program Acquisition Manuals" or "Program Management Guides," which are used as basic texts in explaining, training, and directing personnel in the policies, methods, and procedures of system acquisition and program management. Such revisions should specifically include the concept of application and tailoring of specifications and standards; how, when, and where such application and tailoring should be accomplished; by whom; and the benefits to be derived.

B. Service school and training curricula should be reviewed and revised to include blocks of instructions dealing with the policies and procedures governing the application and tailoring of specifications and standards. This would be particularly true of those courses of instruction that deal with program management, systems acquisition, preparation, maintenance, and use of specifications and standards, as well as those specialized areas such as configuration management, data management, reliability, quality assurance, system safety, and human factors engineering.

VIII. EFFECTIVE DATE AND IMPLEMENTATION

This Directive is effective immediately. The Standardization and Support Directorate under the Office of the Assistant Secretary of Defense (Installations and Logistics) is designated to provide guidance and assistance in the implementation of these policies. Two copies of implementing regulations shall be forwarded to the Assistant Secretary of Defense (Installations and Logistics), attention: MA/WS, within 90 days.

CW Duncan Jr
Deputy Secretary of Defense

Enclosures - 2
1. The Application/Tailoring Process
2. Specifications/Standards Application Record

THE APPLICATION/TAILORING PROCESS

A. The basic process in the application and tailoring of specifications and standards to a given need involves four steps (1) the selection from the total realm of specifications and standards of those documents that may have application to a particular acquisition program; (2) a review and evaluation of these to select the documents that have a specific application; (3) tailoring each of these documents to include only those provisions (sections, paragraphs, or sentences) required for the specific application so that each document imposes only the minimum necessary requirements in the solicitation/contract, and (4) an examination of the document requirements that survive this process to specifically tailor them to support the particular system during acquisition and life cycle ownership.

B. The process described is particularly applicable in the selection and use of nonproduct specifications and standards in a given materiel acquisition program. On the other hand, product specifications such as those for parts, materials and components, are not as susceptible to tailoring when selected for use in a materiel acquisition, since they have been developed around a specific set of design and/or performance characteristics. The process of tailoring the requirements contained in the product specification would normally be accomplished during the development and promulgation of the document, independent of a specific acquisition program. For that reason, the decision regarding the use of product specifications in materiel acquisitions is normally a matter of adopting it in full or rejecting it completely. This does not mean that product specifications cannot be tailored for use in a particular acquisition program. They can and should be when conditions warrant such action.

C. A coequal with the importance of tailoring is the timing in invoking requirements during acquisition. A requirement that is invoked prematurely can incur unnecessary costs, as can a requirement that is not invoked at the appropriate milestone.

D. When engaged in the tailoring process, a degree of caution must be exercised in achieving the desired balance between performance and life cycle cost. While it is essential that specifications and standards be applied in a prudent and cost-effective manner, at the same time they must be properly structured to assure that essential operational capability requirements are not sacrificed.

E. As a collateral matter, in the case of weapon systems or programs that are of interest to more than one Service, extreme caution must be exercised during the tailoring process to assure that each Service's essential needs are met. This is particularly true in matters such as operational requirements, system interface, interoperability and logistics support.

SPECIFICATIONS/STANDARDS APPLICATION RECORD

A permanent record shall be maintained as a management review tool documenting the manner and degree in which the referenced specifications and standards have been tailored as required in subsection VI.E. This record shall:

A. Identify the system or equipment and corresponding Solicitation/Contract Number.

B. Identify and list separately by number and title each document that is cited in the System Specifications and Statement of Work.

C. Provide the following information for each document:

1. Identify where the document is referenced in the solicitation.

2. List (as a minimum by paragraph number) all requirements appearing in the document which are not applicable and those that have been modified. For convenience, if most requirements in the document are not applicable, list only those requirements that are applicable and have been modified. If all provisions of the document are applicable, so indicate.

3. Provide a simple, short entry for each requirement that has been excluded (i.e., not applicable) or modified, limited to reasons such as the following:

   a. To accommodate state-of-the-art technology.

   b. To accommodate industry capability and/or practice.

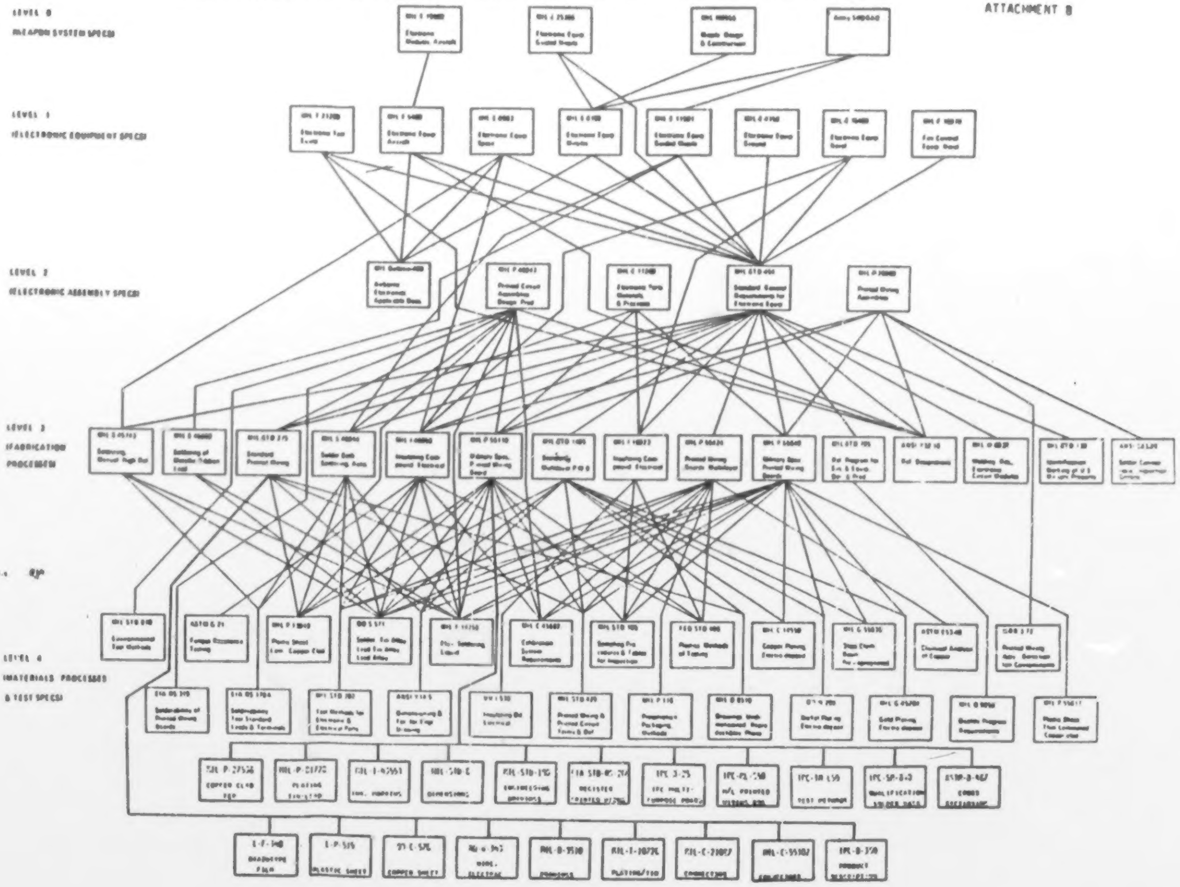
   c. To accommodate the specific system or acquisition phase.

   d. Alteration of requirement to match specific mission, application, or operation.

4. Identify the applicable Data Item Descriptions (Form 1664) and whether these have been tailored to conform to the governing document.

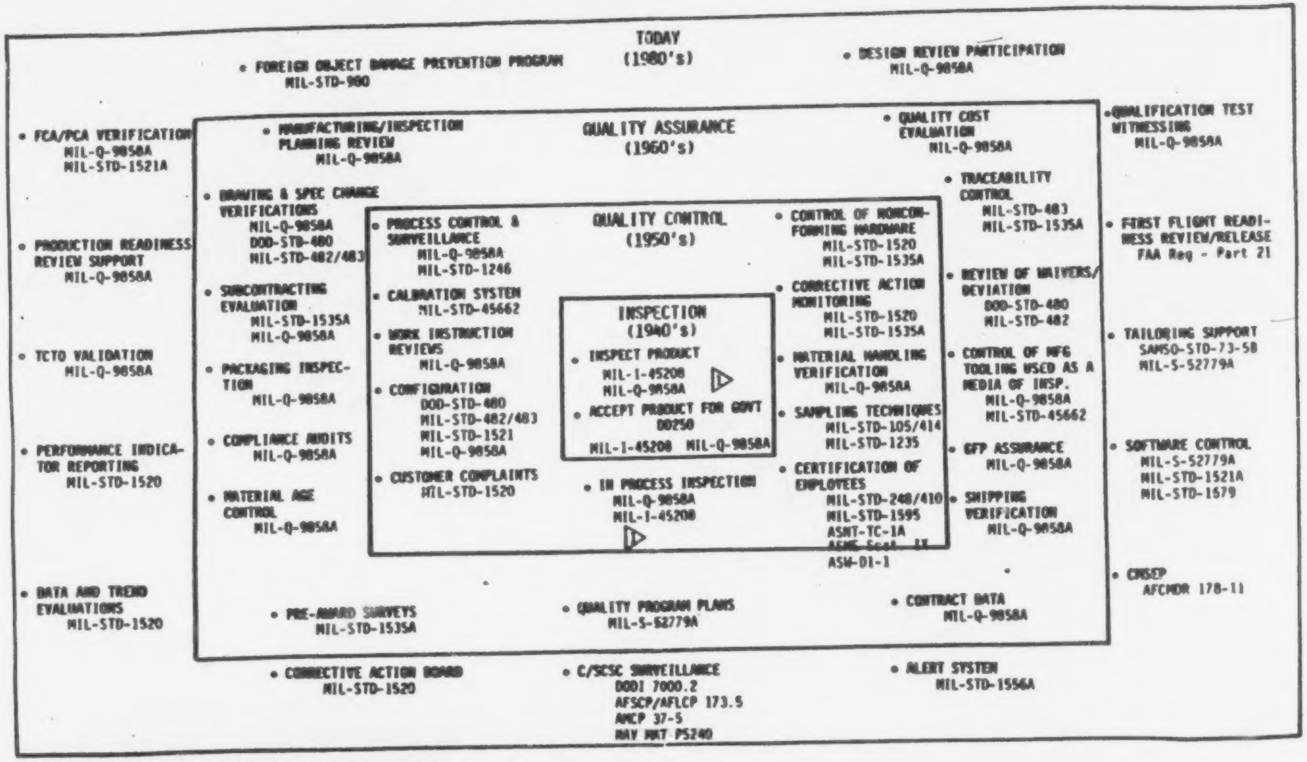
ELECTRICAL\ELECTRONIC MILITARY SPECIFICATION BASELINE

ATTACHMENT B


LEVEL 0
(WEAPON SYSTEM SPECS)
LEVEL 1
(ELECTRONIC EQUIPMENT SPECS)
LEVEL 2
(ELECTRONIC ASSEMBLY SPECS)
LEVEL 3
(FABRICATION PROCESSES)
LEVEL 4
(MATERIALS PROCESSES & TEST SPECS)
COPPER CLAD
PLATING
IPC-TM-650
TEST METHODS
COPPER SHEET
PLASTIC SHEET
CONNECTORS
IPC-D-350
PRODUCT DESCRIPTION

ATTACHMENT C

QUALITY ASSURANCE DEPARTMENTAL REVIEW



TODAY
(1980's)

- FOREIGN OBJECT DAMAGE PREVENTION PROGRAM
  MIL-STD-980
- DESIGN REVIEW PARTICIPATION
  MIL-Q-9858A
- FCA/PCA VERIFICATION
  MIL-Q-9858A
  MIL-STD-1521A
- PRODUCTION READINESS REVIEW SUPPORT
  MIL-Q-9858A
- TCTO VALIDATION
  MIL-Q-9858A
- PERFORMANCE INDICATOR REPORTING
  MIL-STD-1520
- DATA AND TREND EVALUATIONS
  MIL-STD-1520
- CORRECTIVE ACTION BOARD
  MIL-STD-1520
- C/SCSC SURVEILLANCE
  DODI 7000.2
  AFSCP/AFLCP 173.5
  AMCP 37-5
  NAV MAT P5240
- ALERT SYSTEM
  MIL-STD-1556A
- QUALIFICATION TEST WITNESSING
  MIL-Q-9858A
- FIRST FLIGHT READINESS REVIEW/RELEASE
  FAA Reg - Part 21
- TAILORING SUPPORT
  SAMSO-STD-73-5B
  MIL-S-52779A
- SOFTWARE CONTROL
  MIL-S-52779A
  MIL-STD-1521A
  MIL-STD-1679
- CMSEP
  AFCMDR 178-11

QUALITY ASSURANCE
(1960's)

- MANUFACTURING/INSPECTION PLANNING REVIEW
  MIL-Q-9858A
- DRAWING & SPEC CHANGE VERIFICATIONS
  MIL-Q-9858A
  DOD-STD-480
  MIL-STD-482/483
- SUBCONTRACTING EVALUATION
  MIL-STD-1535A
  MIL-Q-9858A
- PACKAGING INSPECTION
  MIL-Q-9858A
- COMPLIANCE AUDITS
  MIL-Q-9858A
- MATERIAL AGE CONTROL
  MIL-Q-9858A
- PRE-AWARD SURVEYS
  MIL-STD-1535A
- QUALITY PROGRAM PLANS
  MIL-S-52779A
- CONTRACT DATA
  MIL-Q-9858A
- QUALITY COST EVALUATION
  MIL-Q-9858A
- TRACEABILITY CONTROL
  MIL-STD-483
  MIL-STD-1535A
- REVIEW OF WAIVERS/DEVIATION
  DOD-STD-480
  MIL-STD-482
- CONTROL OF MFG TOOLING USED AS A MEDIA OF INSP.
  MIL-Q-9858A
  MIL-STD-45662
- GFP ASSURANCE
  MIL-Q-9858A
- SHIPPING VERIFICATION
  MIL-Q-9858A

QUALITY CONTROL
(1950's)

- PROCESS CONTROL & SURVEILLANCE
  MIL-Q-9858A
  MIL-STD-1246
- CALIBRATION SYSTEM
  MIL-STD-45662
- WORK INSTRUCTION REVIEWS
  MIL-Q-9858A
- CONFIGURATION
  DOD-STD-480
  MIL-STD-482/483
  MIL-STD-1521
  MIL-Q-9858A
- CUSTOMER COMPLAINTS
  MIL-STD-1520
- IN PROCESS INSPECTION
  MIL-Q-9858A
  MIL-I-45208
  ▷
- CONTROL OF NONCONFORMING HARDWARE
  MIL-STD-1520
  MIL-STD-1535A
- CORRECTIVE ACTION MONITORING
  MIL-STD-1520
  MIL-STD-1535A
- MATERIAL HANDLING VERIFICATION
  MIL-Q-9858A
- SAMPLING TECHNIQUES
  MIL-STD-105/414
  MIL-STD-1235
- CERTIFICATION OF EMPLOYEES
  MIL-STD-248/410
  MIL-STD-1595
  ASNT-TC-1A
  ASME Sect. IX
  ASW-D1-1

INSPECTION
(1940's)

- INSPECT PRODUCT
  MIL-I-45208
  MIL-Q-9858A ▷
- ACCEPT PRODUCT FOR GOVT
  DD250

MIL-I-45208 MIL-Q-9858A

▷ MIL-STD-453, -454, -883, -1546, -1537, -1540A, -1568A, -271
NHB 5300.4 (Series) - Similar to MIL-Q-9858A
FED-STD-151, MIL-STD-248, MIL-W-8611, MIL-P-51106
MIL-C-6021H, MIL-A-21180, MIL-S-45743
MIL-I-6870, -8950, MIL-G-45204, MIL-S-46044, MIL-W-8604
ASW-D1-1, MIL-W-6858, MIL-S-45060, MIL-W-45205

ATTACHMENT D

THE DEPUTY SECRETARY OF DEFENSE
WASHINGTON DC 20301

3 JUN 1985

MEMORANDUM FOR SECRETARIES OF THE MILITARY DEPARTMENTS
CHAIRMAN, JOINT CHIEFS OF STAFF
UNDER SECRETARIES OF DEFENSE
ASSISTANT SECRETARIES OF DEFENSE
GENERAL COUNSEL
INSPECTOR GENERAL
ASSISTANTS TO THE SECRETARY OF DEFENSE
DIRECTORS OF DEFENSE AGENCIES

SUBJECT: Acquisition Streamlining

As you know, I am placing significant emphasis on meaningful implementation of acquisition streamlining. It is vital that we streamline solicitations and contracts to eliminate counterproductive and overspecified requirements. Although the DoD Directive on acquisition streamlining will be issued shortly, there are aspects of this policy, dealing with the contractual referencing, that require immediate implementation.

One goal of the acquisition streamlining approach is to ensure our contract requirements result from intent and not accident. Failure to place a limit on the contractual applicability of documents referenced in our specifications and standards is a leading contributor to the accidental incorporation of unnecessary or counterproductive contract requirements. We cannot afford resources wasted because of unnecessary requirements.

It is DoD policy to avoid the premature application of military specifications and standards and to limit the inadvertent establishment of contract requirements through indirect referencing. To implement this policy, the following procedures shall be followed:

a. At the onset of development, specify system-level requirements in mission performance terms. Prior to full-scale development, military specifications and standards shall be cited for guidance only. These documents shall be evaluated and, if required, tailored for application to full-scale development.

b. For full-scale development contracts, limit contractual applicability of specifications, standards, and related documents to those cited in the contract and specified portions of documents directly referenced (first-tier references). All other referenced documents (second-tier and below) shall be for guidance only, unless specifically called out in the contract.

c. For production contracts, those specifications, standards, and referenced documents to whatever tier was identified as the baseline for production shall be considered contractual requirements for procurement and reprocurement purposes. Acquisition streamlining should continue throughout the production phase with emphasis on ensuring that only essential requirements are carried forward into follow-on production contracts.

d. When there is a decision to use items already developed such as standard parts and off-the-shelf items, all specifications and standards that define the production baseline for the items are contractually applicable, irrespective of the acquisition phase.

Contractors shall be required, under the terms of the contract, to provide recommendations for application and tailoring of contract requirements in one phase, for proposed application to the succeeding phase. As acquisition programs evolve through demonstration/validation and full-scale development, additional lower-tier specifications and standards will normally be selected and tailored for the next phase. For example, during demonstration/validation certain second- and third-tier referenced documents may be identified as requirements for full-scale development. If so, these lower-tier requirements should be tailored, as appropriate, and identified as requirements in the full-scale development contract. All requirements related to design, development, and manufacturing should be identified and confirmed by the time of the critical design review.

The Government program manager will make the final determination on what contract requirements should apply. DoD Directive 4245.7, "Transition from Development to Production," shall be utilized as a basis for resolving risk and ensuring development of a fully-integrated, producible, and supportable system.

The above policy and guidance shall be applied to existing acquisition programs identified to implement acquisition streamlining and shall be implemented in solicitations and resulting contracts for the development of new systems and equipment issued after September 30, 1985. During the period of initial implementation, there may be a few instances where variations to the above policy and procedures may be warranted. In those instances variations may be authorized by the program manager. However, I would like compliance with this policy and guidance to be a topic for review by the Defense Systems Acquisition Review Council and at Service System Acquisition Review Council reviews.

Request that the policy and guidance contained in this memorandum be provided to the appropriate field system acquisition activities, pending formal publication in DoD Directive 4120.21.

William H. Taft

William H. Taft, IV

SHoo, [illegible]

NATIONAL TOOLING &
MACHINING ASSOCIATION

9300 LIVINGSTON ROAD, FT. WASHINGTON, MD 20744

December 5, 1985

Honorable Dan Quayle
Chairman
Subcommittee on Defense Acquisition Policy
Committee on Armed Services
United States Senate
222 Russell Senate Office Building
Washington, D.C. 20510

Dear Mr. Chairman:

I am writing to correct a misstatement made in my November 13, 1985 testimony before your subcommittee.

My statement says at page 4 that "Only about 10% of the $22 billion in spare parts procurement were openly competed." In reference to this statement Senator Levin asked what was meant by "open competition." I incorrectly responded formal advertising. What I meant by open competition was the percentage of parts purchased by DoD which can be purchased without vendor and/or product prequalification. Such openly competed contracts are both formally advertised and negotiated.

The source of these statistics is a report entitled "IMSS-11 ACQUISITION METHOD/ACQUISITION METHOD SUFFIX CODES" which is compiled on a quarterly basis by the Defense Logistics Agency. The September 1985 edition is enclosed for your reference along with the key to acquisition method suffix codes appearing in applicable DoD regulations. DFARS Supplement No. 6 §S6-201.2.

Only those parts coded "G" under the DoD Replenishment Parts Breakout program are competed without prequalification requirements. A "G" code which results in open competition is assigned where "The Government has unlimited rights to the technical data, and the data package is complete." DFARS Supplement No. 6, §S6-201.2(g). The summary appearing on page one of the report indicates that of the 4,441,360 parts purchased by DoD only 470,050 (10.6%) are coded "G" and purchased without prequalification requirements. Although we have been unable to obtain statistics from DoD, our experience indicates that the percentage of dollars spent on "G" coded items is a fraction of the percentage of parts coded "G".

The dollars spent for parts coded other than "G" is also important to determine where the Government should allocate its resources to best foster competition. For example parts are coded "H" where "The Government physically does not have in its possession sufficient, accurate or legible data to purchase ... [a] part from other than the current source(s)." DFARS Supplement No. 6, §S6-201.2(h). Items coded "H" are relatively easy to break out to open competition but DoD has no record of the amount expended annually on "H" coded items.

When DoD provides the Congress with statistics concerning "competition" for spare parts contracts they do not mean open competition but restricted competition with mindless prequalification requirements. In order to get a true picture of the extent of competition for DoD spare parts contracts, and what steps should be taken to foster competition a breakdown of spare parts expenditures by acquisition method suffix code is needed. We suggest that the Committee request that DoD provide such a statistical breakdown.

If you have any questions, or if we can be of assistance, please let me know.

Sincerely,

Bruce N Hahn

Bruce N. Hahn
Manager, Government Affairs
and Public Relations

Enclosures (2)

(NOTE: Enclosures retained in the files of the Subcommittee on Defense Acquisition Policy.)

American Electronics Association
Government Operations Office

AEA

1612 K Street N.W.
Washington, D.C. 20006

November 21, 1985

The Honorable Carl Levin
SR-459 Russell Senate Office Building
Washington, D.C. 20515

Dear Senator Levin:

AEA was honored to testify before the Defense Acquisition Policy Subcommittee last week regarding the effects of procurement reform legislation and regulations on the defense procurement community.

Per a request made by Senator Quayle during the hearings, I have sent questionnaire to AEA's Government Procurement Committee soliciting examples of specific laws and/or regulations which impose unnecessary administrative and cost burdens on contractors. I will send you AEA's response to this request as soon as it is ready.

In the meantime, you may be interested in reading AEA's testimony which cites several examples of specific laws, regulations and other restrictions which discourage the further use of competition in government procurement. The testimony concludes that competitive contracts are being subjected to the same kinds of procedures that are found in other than competitive contracts as a result both of laws and their implementation. AEA also recommends several steps that can be taken by Congress to improve the defense acquisition process in ways which will encourage competition and thereby reduce defense procurement costs and lead times.

Additionally, AEA appreciates the opportunity to respond to your request for comments regarding S.1783, which you introduced to clarify Congressional intent regarding "work measurement" standards. I have sent your bill and Congressional Record statement to our Procurement Committee for comment which I will send to you as soon as possible.

I should note, however, as Mr. Lightner pointed out during the hearings, the work measurement amendment to the Defense Authorization Act is yet another example of applying regulatory restrictions to all contractors, whether they are competitive or not. There is no exemption for competitive contracts (as AEA recommends in its testimony) from this or any other of a host of legislative and regulatory requirements. While your bill would improve the Act's language, it still represents an effort by Congress to write regulations, regardless of the type of contract being performed. If there are problems with the amendment, why should it be enacted at all, rather than simply delaying its enactment by 180 days?

Again, AEA is honored to have been given the opportunity to testify before the Defense Acquisition Policy Subcommittee. We will be pleased to meet with you at any time to discuss any matters of interest to you.

Sincerely,

Geoffrey A. Feiss
Manager, Government Affairs

American Electronics Association
Government Operations Office

AEA

1612 K Street N.W.
Washington, D.C. 20006

January 20, 1986

The Honorable Dan Quayle, Chairman
Subcommittee on Defense Acquisition Policy
Senate Armed Services Committee
222 Russell Senate Office Building
Washington, D.C. 20510

Dear Senator Quayle:

During hearings you held last November on the subject of procurement reform, AEA was requested to elaborate on those statutes and regulations which we believe are costly and burdensome and which could be eliminated or modified. AEA is honored to have the opportunity to provide the attached response.

AEA is the largest trade association of this nation's largest manufacturing industry. Last year, AEA conducted a government contracting survey of its membership of nearly 3,000 high technology electronics manufacturers. Over 400 companies responded. The results showed that 42 percent of the respondents performed prime contracts for the federal government. The value of such contracts represented an average of 34 percent of the sales of those companies. Additionally, 63 percent of the respondents performed government subcontracts representing an average of 23 percent of the sales of those companies.

The conclusion we draw from these figures is that a very substantial proportion of high technology electronics manufacturing companies performs government prime contracts or subcontracts. However, these companies are primarily commercial. Government contracts represent only a minority fraction of their sales. This is an extremely important fact to keep in mind in analyzing the electronics industry perspective on procurement policy.

We believe that both laws and regulations governing the government procurement process are deviating with increasing regularity from the procedures governing the commercial marketplace. We recognize that there are situations which are unique to the federal marketplace and which require special procedures. But these situations should be more the exception than the norm. The more regulated the government procurement process becomes, the more it deviates from commercial procedures and the more it discourages the very benefits inherent in the competitive commercial marketplace.

AEA's November 13 testimony before your Subcommittee, presented by Jim Lightner, Chairman of Electrospace Systems, Inc., outlined many of the electronics industry's concerns about current laws, regulations and other factors governing the defense acquisition process. It also contains several recommendations which we believe would improve the process and thereby encourage competition while saving the government (and the taxpayer) money.

The following comments are intended to elaborate on those concerns and to provide additional information about laws and regulations which AEA's November testimony did not fully address.

While these comments mention several specific laws and regulations which add unnecessary time and expense to government acquisitions, there appears to be an ever-growing list of additional obstacles to efficient management of the procurement process. Cumulatively, these burdens deter efficiency and quality. The taxpayer ultimately ends up paying higher prices while receiving few benefits, especially in the case of commercial, competitive and fixed price contracts.

If the attached list demonstrates anything, it is that the government (Congress and Executive agencies) tends to regulate first--at any tier, for seemingly any reason--rather than to deregulate. There is an institutional bias throughout the government toward regulation. But there simply is too much regulation. Regulation, by definition, curtails free market processes which encourage variety, innovation, quality and efficiency.

The procurement process needs to be examined strategically. Regulation, wherever possible, should be eliminated. We commend your Committee's outstanding efforts in reviewing the procurement system.

AEA would be happy to assemble a group of industry senior executives to discuss at your convenience these or any other matters of interest to you.

Sincerely,

Dick Iverson

J. Richard Iverson
President

January 22, 1986

PUBLIC PARTICIPATION IN THE LEGISLATIVE AND REGULATORY PROCESS

Problem: Major laws have been enacted effecting work standards, rights in technical data, warranties, certifications of overhead and other cost and price information, etc. with few (if any) hearings. Even more regulations have been promulgated without any opportunity for public comment, despite a requirement in the Competition in Contracting Act for a 30-day public comment period. Laws should be written to withstand the test of time. It should take time to write laws, and it should take more time to implement them.

Solution: Congress simply should not enact laws which have not been the subject of extensive hearings. Further, Congress should prohibit the promulgation of any regulation which has not been made available for at least a 30-day public comment period. We also note that 30 days often is not enough time in which to review adequately the potential effects of a proposed regulation. Therefore, the public comment period requirement should be extended to 60 or 90 days. All affected parties should have an opportunity to review thoroughly and comment on any law or regulation potentially governing their activity.

GOVERNMENT-WIDE ACQUISITION POLICY

Problem: The Federal Acquisition Regulation (FAR) is intended to apply a uniform set of procedures to the procurement of goods and services by the federal government, including all of its departments and agencies. In practice, however, there is little or no uniformity in acquisition procedures. Every Executive department and many agencies have their own "supplements" to the FAR. The Department of Defense FAR Supplement (DFARS) is practically as large as the FAR itself. The military services within the DoD in effect have their own supplementary supplements which frequently deviate substantially from the FAR and even from DoD policy. The Navy, for example, recently issued new acquisition policy without public comment (see below) which violates the FAR. The Air Force also has recently issued a proposed regulation regarding indemnification of contractors (see below) which contradicts the FAR.

Solution: The acquisition policies of Congress, the Pentagon and its military services, and all federal departments and agencies must be coordinated; and discrepancies from the FAR must be held to an absolute minimum. There frequently is little or no reason for agency supplements. In this regard, the authority of the Office of Federal Procurement Policy (OFPP) to coordinate government-wide acquisition policy should be reaffirmed.

LACK OF DIFFERENTIATION BETWEEN WEAPON SYSTEMS AND OTHER ITEMS

Problem: The FAR and its various supplements and supplemental supplements cover procurements that range from major weapons systems to small parts. We understand that much of the current procurement legislation is intended to apply to weapons systems. However, the combined effect of laws and regulations governing procurement is to include commercial products and weapons systems under the same umbrella.

Solution: Laws and regulations governing the acquisition process should clearly differentiate weapons systems and other items. One set of procedures should cover weapons systems and equipment acquired non-competitively. Another set of procedures should cover commercial items and other competitively acquired equipment. The latter should be simple to use, without the paperwork and justifications needed in a multi-billion dollar weapon system. Such a differentiation would encourage competition and increase the supplier base.

DISREGARD FOR "FULL AND OPEN COMPETITION"

Problem: Public Laws 98-369 and 98-577 call for "full and open competition." We understand competition to encompass not only price, but delivery schedule, supportability, technical characteristics of the product, reliability, past performance and other factors affecting the price and quality of the item being procured. However, we find that although contracts meet "full and open competition" standards, the buyer often (subjectively and unilaterally) decides there may not be "adequate price competition." For example, the most recent draft of regulations regarding certification of commercial pricing states that contracts awarded on a basis of other than full and open competition require a pricing certification. It then adds that a certification also is required "where adequate price competition does not exist **despite full and open competition.**" (emphasis added.) This results in contractors being asked to provide all of the information (and potential audit requirements) that would be needed to justify a sole source contract. The commercial contractor may be burdened with unnecessary proposal costs and the government will of course review whatever is submitted.

This problem also exists where prime contractors who have been awarded firm fixed price contracts ask suppliers to provide pricing data and comply with all the rules that apply to sole source contracts. As a result, the supplier, the prime and the government all incur unnecessary administrative costs.

Solution: Any requirement for cost or pricing data should not be imposed in contracts where "full and open competition" exists. Further, when the prices are firm fixed price, there should be no need for any cost data. Only good commercial buying practices need to be followed for lower tier purchases of commercial items.

LACK OF CONTRACT MANAGEMENT

Problem: There are too many cooks in the procurement kitchen. Contract officers, who at least theoretically have overall authority to negotiate contracts for the government, are either unable or unwilling to exercise their authority. Instead, competition advocates, breakout officers, small business advocates, auditors, and a variety of other "specialists" effectively can hold up entire contracts for their own separate causes. As a result, there is a complete breakdown in efficient contract negotiation procedures. There is no control over the contract and nowhere to go to gain control.

Solution: Congress should reaffirm and enforce the authority of the contract officer to oversee and manage the contract negotiation process. Government contracts, and contract officers, should be judged on their overall value to the government, not on a myriad of individual "goals" set independently of the factors which collectively contribute to successful contractual relationships.

LACK OF A COORDINATED AUDIT POLICY

Problem: AEA testified before your subcommittee on March 12, 1985, regarding duplicative and redundant audits and reviews being conducted at contractor facilities. This testimony included several case studies provided by AEA member companies. More recently, the president of one AEA member company wrote to us about a review of government audit activity that his company incurred in 1985:

> [We] had 104 audits (two per week) totalling 238 audit days! Unfortunately, we can't zone defense these audits; we have to play them man-to-man with top level talent. Considering our preparation and follow-up actions from these audits, we effectively have several high cost individuals of different disciplinary skills working full time to meet the regulation driven audit requirements.

Another AEA member company estimates that it costs the company $1.5 million more to meet various audit requirements today than it cost four years ago while yielding the government questionable, if any, benefits.

A specific example of duplicative audits can be found with contractors with over $10 million of negotiated contracts who are following Mil-Q-9858A (dated December 16, 1963). A handbook accompanying the standard instructs government quality assurance representatives to perform a procurement system review. The review covers all portions of the purchasing system. In the late 1970's Section 23 of the Armed Services Procurement Regulation was changed to require a "contractor procurement systems review" when the contractor's negotiated sales were expected to exceed $10 million. This requirement has been carried over to the new FAR Section 44. Thus, contractors are subject to two possibly contradictory procurement system reviews.

Solution: Congress should require DoD to conduct a comprehensive annual audit in each discipline which is sanctioned by all other DoD, government and customer organizations. In the case of the company with 104 audits, this "would reduce the auditing activity to about 5 audits comprising 25 audit days."

WORK MEASUREMENT STANDARDS

Problem: Sec. 917 of the FY 86 Defense Authorization Act would require contractors to maintain "work measurement" standards on defense contracts. The use of work measurement standards met with limited application (mass production, high dollar volume contracts) during the 1940s and earlier; but has since been abandoned as a costly and inefficient management method which damages employee/-employer relationships, and thus, productivity. Sec. 917 would require detailed time and motion analyses to be conducted on **all** production labor (not just "touch" labor) **prior** to production of an item. Thus, any time or labor saving development effected during production of an item would require a new work standard. Contractors would be faced with the specter that the government could allege fraud in cases where cost savings are developed after an item enters full-scale production. Contractors would have little or no incentive to encourage labor savings, and employees would feel that they are being held strictly accountable for every motion they make.

Mil. Std. 1567A imposes similar requirements on contractors, and is equally as counterproductive. The Navy currently is imposing Mil. Std. 1567A on one AEA member company, for example. This company has spent over one year and $400,000 relating to an $8 million labor item on one Navy contract. It has not yet agreed to a single work measurement standard; and it estimates that it eventually will spend $2 million complying with this standard. Similarly, on a $17 million contract, the company estimates it will cost $7.5 million to comply with Mil. Std. 1567A. Further, the company estimates that on an ongoing basis, Mil. Std. 1567A would add 5 percent to the cost of all contracts.

Solution: Sec. 917 of the FY 86 Defense Authorizaton Act should be repealed. Mil. Std. 1567A should be withdrawn; or at the very least should apply only to mass production, high dollar volume, sole source procurements of products where the design is complete at the time the contract is negotiated prior to the award thereof.

PER DIEM TRAVEL COSTS

Problem: The "Federal Civilian Employee and Contractor Expenses Act" (PL 99-234) was amended in the closing hours of the First Session of the 99th Congress to include all government contractors. Earlier last year, the Navy proposed own limitation of contractors' travel expenses. Its proposal, which deviated from the FAR, was expanded when DoD published in the November 20, 1985, Federal Register a proposed clause providing in part that travel expenses exceeding rates "determined by the Administrator of General Services...shall be considered to be not reasonable and unallowable..."

This requirement, either by law or regulation, will force contractors to modify extensively their accounting systems to account for situations where travel costs exceed the standard. The standard itself is, of course, a moving target in that it will change from time to time. Additionally, it is unclear whether the contractor can group all personnel and all travel days in all areas or whether it must be done on an employee-by-employee basis and averaged over the time period involved. Ultimately, the government must bear the burden.

The effect of this requirement will be even more severe on small businesses who may not be able to secure the type of volume discounts that may be available to larger firms or government employees and may not be able to withstand the financial impact of implementing what is, in effect, a government agency type of system.

Finally, the standard is fundamentally unfair. It presumes that each contractor and subcontractor can negotiate rates for every locality on an equivalent basis. It also assumes that contractors can somehow achieve rates that are as favorable as those of the government. There is no vehicle to provide for any contractor comment whatsoever to the Administrator of the General Services when he or she determines these rates. If the government is serious about reducing travel and related costs, then it should negotiate agreements with its major carriers, hotel chains, and the like which allow for contractor use in much the same manner as contractors who are allowed to order GSA catalog items. The fundamental unfairness of this standard also will affect employee morale, productivity and recruiting. In the long run, for this reason alone, it will be self-defeating from a cost standpoint.

Solution: The cost principle and related clause already is adequately covered by the FAR. PL 99-234, at least as it affects government contractors should be repealed, and the proposed DoD FAR Supplement should be withdrawn.

RIGHTS TO TECHNICAL DATA

Problem: During consideration of the FY84 Defense Authorization Act, AEA continually argued that any data rights legislation should contain a specific exemption from acquiring data relating to commercial items (items sold or intended to be sold to the general public). Instead, PL 98-525 merely states that the Secretary of Defense, in issuing implementing regulations, should "consider" whether items are developed at private expense, public expense or some combination thereof. One AEA member company president recently wrote that this requirement "raises the specter that the extensive new product designs we are presently developing will be handed over by our customers to our competition...Recent regulatory changes to demand forfeiture of technical data rights may not promote further competition in our industry and could limit technological developments."

Solution: Congress should explicitly prohibit the acquisition of rights to technical data relating to commercial items.

WARRANTIES

Problem: As noted in AEA's November testimony before your Subcommittee, DoD is insisting on warranties on weapons systems not in mature, full-scale development, contrary to law. This results in extremely drawn out and lengthy negotiations of warranties with increased expense (in both time and cost) to the customer and contractor. There also is evidence that the Pentagon is applying general "standards" to their warranties clauses, regardless of the product or contract involved. Further, AEA continually has argued against applying performance warranties on products not designed or manufactured by the contractor, especially when the product meets government-required specifications. Companies are willing to, and do, provide warranties regularly in the commercial marketplace. The current warranties statute, however, goes beyond a commercial-type of warranty, and as such discourages commercial participation in the federal marketplace.

Solution: Congress should review the warranties statute to ensure that it clearly applies only to products in mature, full-scale development. The statute also needs more appropriately to account for items which are not designed or manufactured by the contractor or which meet government-required specifications. DoD should be prohibited from applying general standards which do not account for the unique circumstances specific to individual contracts.

COST AND PRICING CERTIFICATION THRESHOLD

Problem: As noted in AEA's November testimony, the Competition in Contracting Act lowers the Truth in Negotiations Act cost and pricing certification threshold on defense contracts from $500,000 to $100,000. The $100,000 threshold was established in 1962. Using the producer price index from 1962-1984, the equivalent current dollar threshold would be over $1.6 million. The Pentagon raised the threshold to $500,000 and the General Services Administration was considering doing the same until Congress began debating lowering the DoD threshold back to $100,000. According to DoD testimony before this committee, only 8 percent of DoD procurement expenditures (FYs 82 and 83) involved contracts under $500,000. However, this requirement imposes considerable administrative time and cost burdens on contractors, particularly those smaller contractors who whose business falls under the $500,000 range. Thus, lowering the threshold at best could yield only a small "bang for the buck," while imposing additional administrative costs on small contractors and ultimately the government.

Solution: Congress should raise the cost and pricing certification threshold at least to $500,000 on a government-wide basis.

CERTIFICATION OF COMMERCIAL PRICING

Problem: Proposed federal acquisition regulation (FAC 84-10) implementing Public Laws 98-525 and 98-577 would require contractors to certify that the price offered to the government for commercial items is the lowest offered to anyone else. The proposed regulation far exceeds statutory requirements by applying to all items, not just spare parts, and to all government agencies. Further, the proposed regulation could be applied to procurements using full and open competition, contrary to the law. One AEA member company recently conducted a "test run" on one of its products to gauge the proposed regulation's effect. It took over 40 hours to trace over 400 sales of the product and then to investigate the reason(s) for any prices below that which was offered to the government within the preceeding 60 days (as originally proposed in FAC 84-10). Another AEA member company informs us that it would cost almost $1.7 million to comply with the requirement on a company-wide basis.

Solution: Regulation implementing the commercial pricing certification requirements of PLs 98-525 and 98-577 should apply only to spare parts contracts using other than competitive procedures, as stated in the law.

IDENTIFICATION OF SUPPLIERS AND SUPPLY ITEMS

Problem: Recently issued FAR clause 52.217-7220 requires a contractor to provide for each item to be supplied: 1) the national stock number of the item; 2) an item description; 3) the name and address of the actual manufacturer or each source of supply; and 4) the identification number assigned by each actual manufacturer or source. Such a requirement is wholly inconsistent with commercial practices and the benefits of full and open competition. A contractor providing hundreds of different commercial spare parts, for example, is expected to do all of the research needed to provide this detailed information. No recognition is given to whether the contractor owns the rights to the item being provided or performs other functions such as special inspection after receiving the item. Is the government willing to pay for the effort involved, and if so is it cost effective? If the contractor proposes to charge for this effort and the government does not perceive there is "adequate price competition," the contractor likely will be asked to provide cost data, with the usual audits to follow.

Solution: There is no need for this requirement, especially where full and open competition exists, where the items being procured are available commercially or where the contract involved is firm fixed price.

SECNAV INSTRUCTION 4201.6: POLICY ON NAVY ACQUISITION

Problem: The Secretary of Navy has published an instruction which revives total package procurement, requires contractors to assume cost risks for production tooling and special test equipment, and mandates the use of firm fixed price contracts commencing with the full-scale engineering development point of the program. This instruction, which was not adopted by the other services, will result in higher costs to the DoD, restrict competition and violate DoD regulatory requirements.

The policy requires that contractors assume the cost responsibility for special tooling and special test equipment and suggests recovery of the investment by depreciation, if at all. Assuming a contractor will be allowed to recover the costs eventually, only a deferral occurs. Because contractors will have to secure capital to purchase such equipment, in the long run it will result in increased costs to the Government. Among other factors, prudent contractors will have to ask for additional profit to cover not only the risks associated with financing but with program cancellations as well. Additionally, potential competitors of all sizes will be driven out of the marketplace and will not be willing to take such risks. In the case of small companies (who are acting as subcontractors) they will not be able to secure financing (or will have to pay premium prices for financing) for the equipment. This portion of the policy violates FAR 31.205.40 which provides "...the cost of special tooling and special test equipment used in performing one or more Government contracts is allowable and shall be allocated to the specific Government contract or contracts for which it is acquired..." The Navy policy does not allow for such direct allocation. A depreciation mechanism will in most cases result in a spreading of cost as an overhead item resulting in other agencies not only paying for their special tooling or test equipment but also funding a portion of the Navy's as well.

A second severe problem with the policy is that it requires the combination of significant development and production work in a single contract, pricing them together, which is no more than a variant of total package procurement under DoD Directive 3200.9 which was cancelled in September, 1970 (because the policy was a failure) and replaced by DoD Directive 5000.1. DoD Directive 5000.1 relative to major system acquisitions requires the elimination of substantial development, production, and cost risks before the initiation of firm fixed price contracting. The reasons for current policy are evident. Firm fixed price contracts must by their nature have definitive specifications and work statements in order that they might be realistically priced. An inability to provide definitive specifications results in contractors being forced to include contingencies in their proposals to cover additional risks. It will tend to stifle technical innovativeness in that cost effective tradeoff decisions so necessary to a development effort will not be made. It will also result in the creation of an unhealthy adversarial relationship at a time in a program's life where teamwork between the government and contractor is necessary.

Solution: SECNAV Instruction 4201.6 should be revoked or at least suspended until it can be carefully considered by the DoD as a whole and Congress.

NAVY POLICY ON RELIEF OF SUBCONTRACTORS FROM LIABILITY FOR LOSS OF OR DAMAGE TO GOVERNMENT PROPERTY

Problem: FAR 45.103 provides that subcontractors will be relieved of liability for loss, damage or destruction to Government property under the same circumstances as prime contractors. In a reversal of previous policy, however, the Navy has taken an opposite position

(NAR Supp. 28.303-90) which provides that the Navy "will not take the risk of loss with respect to Government property while in the possession of subcontractors." Limited exceptions do not track the FAR. This has generated numerous subcontractor complaints, as well as extensive loss of time, and consequently additional costs, in fielding and explaining this new requirement.

Solution: NAR Supp. 28.303-90 should be withdrawn. Again, the FAR provides government-wide guidance. A "special" deviation for the Navy, or for the DoD for that matter, is unnecessary.

AIR FORCE STANDARDS FOR INDEMNIFICATION UNDER PL 85-804

Problem: The Air Force recently has proposed (Federal Register, December 4, 1985) standards for Indemnification for Unusually Hazardous Risks under Public Law 85-804. Although, given the history of Air Force delay in approvals, this may be of ultimate benefit, it is also another example of unnecessary agency supplements. In particular, FAR 50.403-1 already provides guidance for indemnification requests. The DoD as a whole (through the DFARS) did not choose to supplement the FAR standard. Yet, the Air Force apparently feels compelled to do so. But for the Air Force informal policy, which seems to discourage approval (without any guidelines), there is no reason for such additional coverage; and, in fact, the purpose appears to make approval of indemnification requests and the entire process much more difficult.

Solution: As noted above, additional supplements such as this defeat the purpose of the FAR, which is to provide for uniform acquisition practices, within all federal agencies. The proposed Air Force supplement should be withdrawn.

IMPROPER CERTIFICATIONS UNDER PUBLIC LAW 96-354

Problem: The Regulatory Flexibility Act of 1980 requires federal agencies to prepare small business impact statements when proposing regulations. However, many if not most proposed regulations give this certification requirement only perfunctory recognition. As an example, in the proposed DFAR guidance on rights to technical data, published in the Federal Register on September 10, 1985, the following "certification" appeared:

> "'DFARS Subpart 227.4 appears not to have a significant economic impact on a substantial number of small entities [and] imposes no new requirements which would require such entities to change their business practices, incur additional costs or otherwise affect their competitive position.'"

Both CODSIA and the AEA, among others, objected to this conclusion. It is inappropriate for such a certification to be made when, in fact, associations representing small business entities vehemently object to it.

Solution: As noted above, both laws and regulations should not be written without thorough prior consideration of effects on all parties. Congress should reaffirm the intent of PL 96-354.

SMALL BUSINESS EXEMPTION FROM COST ACCOUNTING STANDARDS

Problem: Small businesses currently are exempted from the Cost Accounting Standards (FAR 30.301(b)(3)). However, Defense Contract Audit Agency auditors currently require the use of these standards (CAS) when determining "allocability" and "allowability" of costs in accordance with the contract cost principles and procedures of the FAR Part 31. Thus, even though small businesses are exempt from the CAS, they are being applied in order to justify the small business' cost or price proposals in many situations.

Solution: FAR Part 31 should be modified to provide simpler cost principles for application to small businesses, non-profit organizations and educational institutions.

"STATEMENTS OF QUALITY" VERSUS "CERTIFICATE OF CONFORMANCE"

Problem: The Defense Logistics Agency (Manual 8200.1, Sec.V, paragraph 2) instructs the Defense Contract Administration Service (DCAS) quality assurance representatives (QARs) as to what are acceptable "statements of quality". However, the term "statements of quality" is not used in the FAR, or other quality documents. The term used in the FAR (52.246.15) is "certificate of conformance," which in part states "that the supplies or services are of the quality specified and conform in all respects with the contract requirements, including specifications, drawings..." The statement in this clause, which is an acceptable certification as far as the contract is concerned, can be interpreted to be non-acceptable based on the guidance of DLA Manual 8200.1.

Solution: DLA Manual 8200.1 should be revised to conform to the FAR.

[Whereupon, at 11:50 a.m., the subcommittee adjourned, subject to the call of the Chair.]

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